If you have just a few years until you retire, it's wise to double-check

As featured in WORTHWHILE, a quarterly periodical dedicated to serving the clients of Raymond James advisors and affiliated advisory firms.

Retirement comes into sharper focus as it gets nearer, with questions about longevity, health and healthcare, downsizing, relocating, more leisure time, when to take Social Security, and the Big One – will I have enough money? – taking on increasing urgency. We may have had a rose-hued fantasy that sustained us during long hours at work, or we simply may not have thought about what our retirement could look like. At some point, however – probably in our mid- to late-50s – the reality that a new stage of life is just over the horizon starts to sink in. Like marriage or parenthood, it's a stage we can't fully understand until we're in it. But, it's also a stage we should do our very best to prepare for.

Meanwhile, while we've been working, retirement has been changing, and pretty radically. For example, improvements in healthcare have extended life spans and enabled people to remain active and involved far longer than in our parents' day. While that's great, longer life spans also mean that our nest egg had better be robust and a plan for generating reliable, ongoing income needs to be firmly in place. Modern retirement has a lot of parts, and yes, they are moving. But with proper planning, a hearty dose of realism, and a willingness to make course corrections if need be, retirement can be a time of freedom, new beginnings and shortening that bucket list – all underpinned by a solid financial foundation. With that objective in mind, let's look at what's needed to attempt to construct a secure and enjoyable retirement, creating a checklist of questions we need to ask – and answer – to ensure that we're heading in the right direction.

We are indebted to baseball great Yogi Berra for the insight, "If you don't know where you're going, you'll end up someplace else," and that's true with retirement. You can't put in place or fund something you haven't defined, so our first step on the road to a satisfying retirement is to get an idea of what that looks like. While everyone's picture – including a spouse's – will have different details, we need to at least be able to create an overall framework, understanding that we can fill in the specifics as R-day gets closer. At a minimum, you need to have an idea of where you want to live, how you plan to spend your time, and what new goals you want to pursue. One way to start is to imagine an ideal day, week and month. Your retirement is going to involve and affect others, so they need to be part of your dreams and discussions as well.

> With proper planning, retirement can be a time of freedom, new beginnings and shortening that bucket list

Once you have a vision, you can begin to make it a reality by addressing these questions:

Do I understand my expenses?

The biggest anxiety most people have is that they will outlive their money in retirement, so let's tackle that one first. What can cause you to run out of money? Well, not knowing what you're spending and where is obviously asking for trouble, so you need to have a realistic budget that separates needs (housing, food, healthcare, etc.) from wants (travel, entertainment, charitable giving, etc.). While things will change, you need that budget well before retirement arrives so you can make any necessary changes to your spending patterns, as well as any other course corrections (saving more, retiring later, changing your investment strategy) to how you're going to fund the next stage of your life.

Do I understand my sources of income?

Broadly speaking, retirement income can be divided into reliable and assumed sources. Defined benefit pensions – if you're fortunate enough to have one – and Social Security are examples of reliable income. With regard to Social Security, it's critical to understand that the choice you make about when to start taking your benefits determines that income for the rest of your life. Although many people file for their benefits at the earliest eligibility age of 62, those who figure out how to defer taking benefits until the mandatory age of 70 will be eligible for much higher monthly payouts. You also need to weigh the pros and cons of your start date because that will affect survivor benefits for your spouse. Spouses also should investigate strategies to maximize their combined lifetime Social Security benefits – your advisor can tell you more about this.

Since they will fluctuate, income from investment assets such as

Key decision dates as retirement approaches

You will be making a number of age-related decisions – either deliberately or by default – as you get closer to retirement. Since many of them can affect benefits and/or your cash flow during retirement, it's wise to be aware of them, and to coordinate your decisions with a spouse, especially if you are of different ages. Here are some key dates to keep in mind:

Age	Decision
50	Eligible for IRA and 401(k) catch-up provisions
55	Eligible for penalty free separation-from-service withdrawals from 401(k)s
59½	Eligible to begin withdrawing from IRAs and 401(k)s penalty free
62	First eligible for Social Security with reduced benefits
65	First eligible for Medicare
66	Full retirement age (FRA) for Social Security (born 1943-1954; FRA increases by two months for every year from 1955 to 1959)
67	Full retirement age for Social Security (born 1960 or later)
70	Maximum Social Security benefit (you must begin taking benefits)
70½	Required minimum distributions begin the year after you hit this age

Modern retirement lasts longer so your assets and income stream have to last longer, too

Being too conservative with your investments can be as dangerous as being too aggressive

401(k) plans, IRAs, Roth IRAs, brokerage accounts and CDs generally fall into the category of assumed sources. Developing, implementing and monitoring an investment strategy to generate retirement income, while also recognizing your individual tolerance for risk, is best done in collaboration with a financial advisor. The days of "set it and forget it" are long gone. Bear in mind that when it comes to retirement, being too conservative with your investments can be as dangerous as being too aggressive. Selecting an asset allocation strategy that seeks to reduce the risk to your principal, generates income and takes inflation into account is a complex process that requires trust and ongoing communication between you and your advisor. Please remember that asset allocation does not guarantee a profit nor protect against loss.

Have I planned for longevity?

As mentioned, modern retirement lasts longer so your assets and income stream have to last longer, too. For example, if you and your spouse are both 65 when you retire, there's an 85% chance that at least one of you will live beyond 85. During those 20-plus years, inflation is going to drive expenses higher. While you can't quantify factors such as life span and inflation precisely, you need to be aware of them and incorporate them in your planning. Setting realistic goals can help deal with worries that can take a lot of the pleasure out of retirement.

How much of your retirement is owned by Uncle Sam?

Understanding your tax liabilities and options in retirement

As with income at earlier times of life, it's not what you get that matters in retirement, it's what you get to keep. Uncle Sam and his various cousins will be close at hand, so you need to keep tabs on your tax picture. Fortunately, you may have some flexibility in managing the total and the types of income you receive and therefore your tax liability. Let's look at where you can't influence your tax liability – and areas where you can:

RMDs

You don't have much flexibility with required minimum distributions (RMDs) from a 401(k) or IRA – your annual RMD is determined by a formula based on the total value of your retirement account and your life expectancy. RMDs are typically taxed as ordinary income. And whatever you fail to withdraw can be taxed at 50%.

PENSION OR ANNUITY PAYMENTS

If you receive retirement benefits from a pension or annuity payments from a qualified employer retirement plan, all or some may be taxable. It depends on who invested in the contract and how contributions were made. Those payments will be fully taxable if you have no investment in the contract. However, if you contributed after-tax dollars to your pension or annuity, your pension payments are partially taxable – you shouldn't owe tax on the part of the payment that represents a return of the after-tax amount you paid.

SOCIAL SECURITY BENEFITS

For most people, some portion of your Social Security benefits will be taxable, with the percentage determined by what the IRS calls your "combined income," which is your adjusted gross income, plus any nontaxable interest, plus half of your Social Security benefits. For more information, see ssa.gov/planners/taxes.htm.

So far, we've looked at areas that are usually taxed as ordinary income. However, retirees often have multiple sources of income and some of which can offer more flexibility.

There are three primary types of investment accounts: tax-deferred, taxable and tax-free. As discussed, tax-deferred accounts have various rules concerning withdrawals, making them less flexible in terms of managing your tax bracket. For taxable accounts, be sure to consider the tax consequences (short- or long-term) of any securities you sell. Like they sound, tax-free accounts such as Roth IRAs and Roth 401(k)s provide greater flexibility because there are no tax considerations regarding withdrawals when certain conditions are met.

Once you know your baseline taxable income – what's coming from your RMDs, pension plans and Social Security – you can prioritize your other withdrawals while keeping an eye on your overall tax bracket. Generally speaking, after taking your required withdrawals, you should move on to any taxable accounts, while leaving your Roth 401(k) and Roth IRA for last. As always, be aware that each individual's tax picture is unique, and be sure to work closely with your advisor and a trusted tax professional.

Order matters

Where you get your retirement income and the order you spend it could affect your ultimate tax liability. While each person's situation will be different, generally speaking, it's a good idea to spend your reliable income (e.g., RMDs, Social Security and annuity payments) before drawing from taxable accounts. Leave tax-deferred or tax-exempt accounts for later so they can continue to grow.

Retirement isn't static – it changes as you move through it – so your planning should reflect that

How will I handle healthcare costs?

While the healthcare environment is changing, few people believe that their medical expenses in retirement are going to decline. Medicare provides healthcare insurance to most Americans over age 65, but it does not provide complete coverage and it won't cover you if you retire abroad. According to the Employee Benefit Research Institute, Medicare pays only about 60% of current retirees' medical costs. You will be responsible for copays, premiums and deductibles, and Medicare doesn't cover hearing, dental or vision expenses at all. While it's impossible to precisely predict out-of-pocket expenses, a retired couple can easily spend $10,000 a year above and beyond what's covered by Medicare. Multiply that by 20-plus years, and it's easy to see why this area demands attention. What's more, Medicare itself has many moving parts, requiring ongoing decisions not only about the plan's components but also any supplemental healthcare insurance you may want to purchase. Healthcare costs can derail your retirement in a hurry, so you're not ready until you understand Medicare, have thought about your uncovered costs in the context of your medical history, and put in place a personal plan to address healthcare costs that anticipates the effects of inflation. While this may sound daunting, your financial advisor knows the landscape and has helped many people navigate it – get some expert help.

Have I thought about long-term care?

This is another area where planning ahead really matters. The U.S. Department of Health and Human Services estimates that about 70% of those 65 and older will require some type of long-term care during their lifetime. In other words, you're probably going to need long-term

What to do if you're behind

A retirement readiness checklist isn't much use if you don't respond to what it tells you. If your retirement plan isn't on track, the sooner you address matters the better. In most cases, people either haven't saved enough or just don't have a good fix on what retirement is really going to cost. The quicker you bring things into balance, the more time the changes you make have to work. Here are some ideas:

Streamline your lifestyle. If you're behind, you need to look at your expenses, both current and what you anticipate spending in retirement. Cutting costs now can free up money that will enable you to increase your savings, and also help you get accustomed to living on less. See if you can take 5% out of your expenses, and then see if you can cut another 5%. It may not be as hard as you think, and the earlier you do it, the more impact it will have.

Reexamine your portfolio. While you can't make the markets deliver the income you need, a slight change in your asset allocation could mean a bigger nest egg when retirement arrives. Be careful here – if you get too aggressive in reaching for yield or pursuing growth, you could set yourself back significantly if markets falter. Your advisor can help you find the right balance.

care and it's likely to be expensive. Coverage for long-term care is patchwork – Medicare will pay for some home healthcare services but not others, and the government won't help with nursing home costs unless you have depleted your assets. Long-term care insurance is one way of addressing this issue, but you need to shop around because premiums and benefits vary widely – and can change after you purchase a policy. It's easy to put this off, but as a general rule, the earlier you buy, the lower your premiums. Again, your financial advisor has been down this road with others and can help.

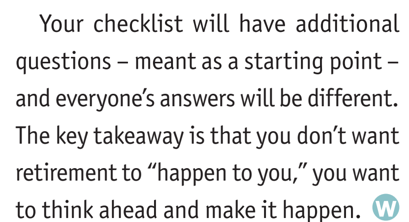
Have I considered my legacy?

Thinking about retirement inevitably leads to thinking about mortality and what we want to leave behind. While this part of the retirement picture will be highly personal, most people want to take care of their loved ones and also want to contribute to organizations whose work they value. Many retirees find meaning in volunteering, and this can be extended by developing an estate plan that benefits groups close to your heart. Of course, estate planning also has tax implications – both for you during retirement and for your beneficiaries later on – so it's another area where expert advice is required.

Do you think you're ready?

One thing to understand is that while retirement is a stage, it also has its own stages. For example, many people want to travel more when they retire, and this is something that usually occurs early on when we can get around better. On the cost side, we're probably going to see our healthcare expenses increase as the years go by. In other words, retirement isn't static – it changes as you move through it – so your planning should reflect that.

Your checklist will have additional questions – meant as a starting point – and everyone's answers will be different. The key takeaway is that you don't want retirement to "happen to you," you want to think ahead and make it happen.



Save more. Easy to say and perhaps hard to do, but your nest egg can only reach the desired level if you put enough money into it. If you're 10 years away from retirement, you may be able to raise your savings rate more gradually; if you're closer in, you'll have to be more aggressive. In any event, take advantage of every tax-deferred opportunity you have, so your money has time to grow. For example, try to max out your 401(k) with up to $17,500 in annual pretax contributions, plus $5,500 in catch-up contributions for those over age 50. You can also open an IRA, with up to $5,500 in annual tax deductible contributions, plus $1,000 in catch-up contributions for those over age 50. Although there's no immediate deduction, a Roth IRA is very useful in retirement because there's no tax liability on certain withdrawals.

SAVE MORE. STREAMLINE YOUR LIFESTYLE. REEXAMINE YOUR PORTFOLIO. RETIRE LATER. RETIRE PART TIME.

Retire later. This usually isn't at the top of anyone's hit parade, but waiting longer gives you more time to accumulate the money you need. A year or two can make a big difference, as can waiting longer before taking your Social Security benefits.

Retire part time. Retirement doesn't have to be either/or. Consider easing into it by staying on with your current employer part time, or finding a job for 20 or so hours a week. Once you reach 65 and are eligible for Medicare coverage, you might find that your employer is amenable to letting you work part time as a consultant. The company no longer has to pay you benefits, but still gets your expertise. You're a bargain! Think about working in retirement since it can provide not only financial rewards but also the camaraderie of colleagues and an ongoing feeling of contributing.

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