WORKING PAST 65

THREE WAYS TO MAKE IT LESS OF A CHORE

You've run the calculations. You've kicked up your savings rate, opened Roth accounts, maxed out 401(k)s, and tweaked your asset allocation to allow for more long-term growth. And despite all of your efforts, you're faced with a bleak scenario: You're going to have to work longer than you had originally hoped.

It might be small consolation, but you're far from alone. Most people hurtling into retirement today won't have the financial safety net of a pension. Yet they haven't amassed enough of their own financial assets to cover their expenses once they retire.

They have only one option left: working longer, provided they're able to do so.

Even if you don't absolutely have to work past 65, numerous studies and retirement calculators clearly illustrate the benefits of continuing to do so. Not only will you continue to collect your paycheck, but you'll also reduce the number of years you'll have to rely on your nest egg, thereby improving the odds it won't run out prematurely. Delaying Social Security past your normal retirement age also means that you'll receive a higher payout from the program.

If you fall into the "work longer" contingent, the thought of setting your alarm for 6 a.m. and packing sack lunches past age 65 might seem downright unappealing. Aren't you supposed to be spending your post-65 years spoiling your grandkids and seeing the sights you didn't have time to see when you were still working?

Maybe. But if you're still healthy and have a job, those are two pluses right there. And there are ways to make working longer more palatable, three of which we've shared below. The unifying theme among all of them is to relax and begin enjoying a happier lifestyle even as you continue to collect a paycheck.

Stop saving

One idea for enjoying the fruits of your labors even as you continue to work comes courtesy of T. Rowe Price. The investment firm found that working longer greatly increased a person's chances of not outliving his nest egg as a result of three factors: continued income, delayed portfolio withdrawals and a larger Social Security check. At the same time, T. Rowe found that the advantages of saving within tax-deferred accounts like a 401(k) aren't especially great for late-career savers. Yes, your money will compound tax-deferred, but the benefits of tax-deferred compounding on new investments aren't nearly as great as they were earlier in your career. Given that data set, T. Rowe asserts that a healthy compromise for many pre-retirees is to continue working but begin spending some of that cash that they had previously been earmarking for their 401(k)s. T. Rowe Price calls it "Practice Retirement."

Start Social Security for one spouse

Two-career couples know how much easier life is on days when one of them is off. No one has to squeeze in walking the dog before work or come home to a dark house. And errands that we normally tackle on the weekends are magically completed. If both you and your spouse are still working, one option to improve both partners' quality of life is for one spouse to stop working while the other one stays on the job.

Assuming the lower-earning spouse is the first to retire, he or she could begin claiming benefits based on his or her own work record at age 62, while the higher-earning spouse delays benefits until age 70. (This strategy is sometimes referred to as the 62/70 split.) The Social Security Administration's website has some extremely useful tools for modeling out various scenarios. (You also can call the Social Security administration or visit a local office if you have specific questions about your own situation.)

Make it a labor of love

If you've logged a long career within a specific field or with one company, staying put for the rest of your working years might deliver the highest financial payout. However, needing to work longer doesn't necessarily mean you have to do the same job you've always done, and staying put in a job you hate may exact a mental and physical toll even while it improves your financial well-being. Morningstar contributor Mark Miller has written extensively about encore careers — those embarked upon after age 50 that tap into a pre-retiree's desire to do a job that offers personal meaning and gratification. Such positions may not offer the same financial rewards that your old 9-to-5 job did, but if you're doing something you love, the trade-off might be worth it.

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RETIREES, ARE YOU SPENDING TOO MUCH?

How much can you spend in retirement without outliving your money? It's one of the most fundamental questions confronting anyone who' has retired — or is getting ready to.

But it's a head-scratcher for many, according to a survey from the American College of Financial Services. Seven in 10 individuals between the ages of 60 and 75 with at least $100,000 said they were unfamiliar with the oft-cited 4 percent withdrawal-rate guideline. Meanwhile, 16 percent of survey respondents pegged 6 percent to 8 percent as a safe withdrawal rate.

That's a problem. Because setting a sustainable withdrawal rate is such an important part of retirement planning, pre-retirees and retirees who need guidance should seek the help of a financial advisor for this part of the planning process.

And at a bare minimum, anyone embarking on retirement should understand the basics of spending rates: how to calculate them; how to make sure their spending passes the sniff test of sustainability given their time horizon and asset allocation; and why it can be valuable to adjust spending rates over time.

How to calculate spending rates

To determine your own spending rate, simply tally up your expenses — either real or projected — in a given year. Subtract from that amount any nonportfolio income that you're receiving in retirement: Social Security, pension, rental or annuity income, to name a few key examples. The amount that you're left with is the amount of income you'll need to draw from your portfolio. Divide that dollar amount by your total portfolio value to arrive at your spending rate.

Say, for example, a retiree has $60,000 in annual income needs, $28,000 of which is coming from Social Security and the remainder of which — $32,000 — she will need to draw from her portfolio. If she has an $800,000 portfolio, her $32,000 annual portfolio spending is precisely 4 percent. But if she needs to draw $50,000 from her portfolio, her spending rate is 6.25 percent.

The 4 percent rule, unpacked

The notion that 4 percent is generally a safe withdrawal rate was originally advanced by financial planner William Bengen. It has subsequently been refined — but generally corroborated — by several academic studies, including the so-called Trinity study. Before retirees take the 4 percent guideline and run with it, however, it's important to understand the assumptions that underpinned it.

First, the research assumed that retirees would wish to maintain a consistent standard of living, drawing a steady stream of income from their portfolios each year. Thus, the 4 percent guideline assumes that the retiree spends 4 percent of his or her initial balance in year one of retirement, then subsequently nudges the amount up in subsequent years to keep pace with inflation. He or she doesn't take 4 percent of the balance year in and year out, though that's a viable spending-rate method, too.

Additionally, the 4 percent guideline assumes a 60 percent equity/40 percent bond asset allocation and a 30-year time horizon, and that the 4 percent, whether it comes from income and dividend distributions or from selling securities, is the total withdrawal. Thus, a retiree whose portfolio was generating 4 percent in income distributions couldn't take an additional 4 percent from her principal.

Swing factors

Because not every retiree's profile matches those parameters, not every retiree should take the 4 percent guideline and run with it. Retirees should be prepared to adjust their spending rates up or down based on the following factors:

Time horizon: Retirees with time horizons that are longer than 30 years should plan to take well less than 4 percent of their portfolios in year one of retirement. On the flip side, older retirees — those 75 or older, for example — might consider taking a higher withdrawal rate. David Blanchett, head of retirement research for Morningstar Investment Management, has suggested that retirees consider their life expectancies when determining their spending rates. The IRS' tables for required minimum distributions from IRAs can help you see the interplay between life expectancy and withdrawal rates.

Asset allocation: A retiree's asset allocation also should be in the mix when calibrating sustainable spending rates. The 4 percent guideline, as noted above, is centered around a 60 percent equity/40 percent bond mix. But investors who want to employ a portfolio that includes more bonds and cash should be more conservative in their spending rates, notes Blanchett. The reason is that bond yields have historically been a reasonable predictor of bond performance in subsequent years, and bond payouts are ultralow right now.

Market performance: The bear market of 2008 illustrated so-called sequencing risk: Retirees greatly reduce their portfolios' sustainability potential when they encounter a lousy market early on in their retirements and don't take steps to reduce their spending. That's because if they overspend during those lean years, they leave less of their portfolios in place to recover when the market does.

Right spending strategy for you

Indeed, much of the recent research on sustainable withdrawal rates supports the idea of tying in withdrawal rates with portfolio performance. The retiree takes less out in down-market years and can potentially take more out in years when the market performs well.

The purest way to tie in spending with portfolio performance is simply to take a fixed percentage of that portfolio — say, 4 percent — year in and year out. Under this method, the retiree could take $32,000 from his or her portfolio when its value is $800,000, but would be forced to live on $24,000 if his or her portfolio dropped to $600,000 in value. Using the fixed-percentage method, the retiree would never run out of money, but he or she might not be able to make do on the smaller amount.

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