



How to Spend Enough in Retirement

By Emily Brandon

Posted December 14, 2007

The financial services industry and the media have apparently done a good job of persuading people that they need to save more for retirement and frightening them that their nest egg won't last. A new survey shows that once retired, most Americans are reluctant to spend their dough.

Three quarters of retirees ages 60 to 75 with at least \$50,000 in household assets say they either kept their nest egg principal intact over the past year or actually added to it, according to an AARP and American Council of Life Insurers survey released this week. Only about one quarter dipped into their savings. "People are so concerned about outliving their nest eggs that they will skimp on certain expenses," says Jean Setzfand, director of AARP's economic issues agenda.

That may be good news for the financial services industry, which collects fees on the more than \$7 trillion in assets held in IRAs and 401(k)'s, but the AARP thinks that retirees shouldn't be afraid to live a little, assuming they have the means and take the time to budget for a long life and the possibility of health expenses.

Here's how you can tap your nest egg while making sure it lasts your lifetime.

Withdraw the appropriate amount. Retirees take a variety of conservative approaches to spending their savings, the survey found. Many withdraw money only for emergencies (23 percent), take only interest, gains, or dividends from savings and investments (14 percent), or withdraw no money at all (13 percent). "Most of our clients don't want to dip into their principal," says Steven Medland, a certified financial planner and partner at TABR Capital Management in Orange, Calif. "For most of our clients, their spending doesn't go down a whole lot in retirement, and it is smart for them to be cautious."

But some financial advisers say it's OK to dip into principal as long as you have a plan to make it last. "That principal is there to be used," says William Reichenstein, a chartered financial analyst and professor of investment management at Baylor University. "You should be working into principal conservatively." The magic number, according to Craig Copeland, a senior research associate at the Employee Benefit Research Institute: "Take 4 percent of your assets out every year, and you can expect to have enough money to last you 25 to 30 years." But only 13 percent of retirees regularly draw down a constant percentage of their nest egg, AARP found.

Spend taxable dollars first. "The rule of thumb is you want to take money out of a taxable account before any other retirement accounts," Reichenstein says. "You want to minimize the tax rate." Tax rates can fluctuate from year to year in retirement if you don't have a steady income stream other than Social Security. So you should take more than the minimum required withdrawal out of your traditional IRA or 401(k)—and pay the extra income tax—in years when you are in an especially low tax bracket or toward the bottom of a tax bracket. "Those tend to occur for most individuals late in their life, if you need to go to a nursing home or if you have high medical expenses. In those years you will probably be in a low tax rate," Reichenstein says. If you can make retirement accounts last, it's also sure to help you cover your medical bills.

Monitor your accounts. Retirees report being very or somewhat concerned about inflation (76 percent) and a decline in the stock market (64 percent), AARP found, and rightly so. "You don't know what future returns will be, and those healthy returns of the past few years don't always hold up," Reichenstein says. So, many retirees make timid investment choices. If the value of their investments dropped by even 5 percent, nearly two thirds of retirees would change their spending the next year.

But some retirement experts believe you still need to take a bit of risk with your portfolio in the early years of retirement if you want that money to last as long as you live. "Most people who are in their older age go to bond or money market type investments," Copeland says. "There is a need to invest in stocks for longer. If you're healthy and you have good genes, you can expect to live 20 years [in retirement]. You don't want to be 90 percent in fixed investments." And if you do happen to have a good year, tuck the money away for leaner times. "Even if the account is up 5 or 10 percent in a decent year, you want to keep the return of that at work for you for a rainy day, because there are going to be other accounts that aren't doing as well," says Medland.

Plan for unexpected expenses. Some 63 percent of retirees also worry about having to pay for healthcare and prescription drugs, AARP found. And about a third think it will be difficult to keep enough money for needs in later life. Long-term care insurance can help, but, just like when you're working, it's a good idea to have an emergency fund to help you through rough spots. When spending down your nest egg, "you still want to leave a safety margin," Medland says. "Because you could live to be 100."