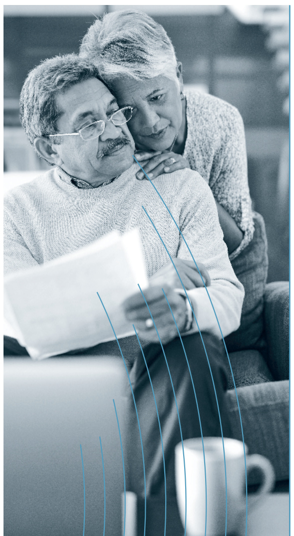
# Modern Retirement: Potential Areas of Trouble



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**AS A CERTIFIED FINANCIAL PLANNER™,** much of my social life is occupied with answering the financial questions of friends, family and acquaintances with phrases like "it depends" and "maybe." No universal advice is applicable to every person in every situation. Further, my inability to answer questions definitively is amplified as retirement nears for the person asking the questions.

Given the unique characteristics of every family, conducting a detailed retirement feasibility study is imperative as anyone nears retirement. This need is likely increased in today's environment as interest rates on cash flowing vehicles like bonds and CDs are at historically low levels, and questions abound regarding the sustainability of our current economic expansion.

While a detailed examination of personal financial circumstances is crucial, the following areas might prove troublesome for today's newly minted retirees and should be considered carefully when creating a financial plan moving forward.

## HEALTHCARE EXPENSES

Fidelity recently published a study that estimates the average married couple, aged 65, will need $285,000 in current portfolio dollars to cover medical expenses[1.] (This does not include long-term care, but more on that momentarily.) This is undoubtedly one of the largest expenses in retirement for most retirees. While the Medicare program, when paired with supplements, can provide high-quality medical insurance coverage, the costs associated are significant and need to be planned for accordingly. I've had multiple clients who feel like they are all set when they reach Medicare age (65) only to be taken aback by the costs of coverage.

One avenue to counteract the drag of medical expenses in retirement is to consider a Health Savings Account (HSA) in your final working years before retirement. This highly tax efficient vehicle is only available to individuals with a high-deductible health plan but can be used to offset future retirement medical expenses.

Long-term care expenses are a particularly challenging topic for retirees. Premiums for insurance coverage to protect against this risk have increased substantially over time. Hybrid policies have some great attributes but also carry meaningful costs and some disadvantages. While no easy answers exist for the long-term care conundrum, it is important to be aware of the potential for significant costs in the future and to consider alternatives as early in the retirement planning process as possible.

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## INCOME TAXATION

For many retirees, retirement brings relief from tax burdens when their high earning years of employment are in the past. Many, however, find themselves in higher tax brackets than anticipated.

One area of surprise for many is the taxation of Social Security income. For a married couple in 2019, a combined income (Adjusted Gross Income (AGI) + nontaxable interest + 50 percent of Social Security Income) greater than $44,000 causes taxation of 85 percent of Social Security benefits. It is not uncommon for a married couple to receive Social Security income of greater than $50,000 per year, and it is likely that they should expect to pay income tax on 85 percent of that amount.

Typically, one of the largest areas of taxation in retirement is on qualified (pre-tax) retirement plan distributions. These can occur before the age of 70½ to support lifestyle spending needs or can occur after 70½ to support lifestyle and/or to fulfill Required Minimum Distributions (RMDs). Smoothing out future tax liabilities through techniques such as Roth Conversions can assist in planning for this potential tax issue.

## INFLATION

Inflation is commonly overlooked due to the small year-over-year changes typically experienced. Further, inflation has been running near or below two percent for some time. Still, two percent inflation over the course of a lengthy retirement eats away significantly at the spending power of your savings. I still remember when my parents purchased a 1988 Mercury Topaz and couldn't believe the day had come where they spent $10,000 on a vehicle. Thirty-one years later, while new car costs might not have fully appreciated at the rate of inflation, no new vehicle is available at such a low price point. Some allocation to assets that can out-pace inflation (such as stocks) are typically needed to achieve a successful retirement outcome.

## STOCK MARKET VOLATILITY

Given the tremendous stock market gains enjoyed since The Great Recession of 2008, many portfolios have appreciated significantly and are higher today than could have been traditionally expected. Unfortunately for those retiring today, higher valuation and the potential future slowing of the economy might lead to increased market volatility in the coming years. As noted above, given the inflationary issues inherent in a lengthy retirement, taking on some risk may still be warranted in a retiree portfolio. It is important, however, that less volatile assets, such as fixed income, also be included in retiree portfolios to draw from during periods of poor stock market performance.

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## INCREASED SPENDING IN EARLY RETIREMENT YEARS

Financial planning expert Michael Kitces has documented the lack of linear spending patterns for retirees[2]. He's coined the first 10 years as the "Go-Go" years, insinuating spending levels higher than expected as retirees spend on items they might have been waiting to experience previously, but never had the time. While not unusual or even necessarily problematic, these spending patterns need to be carefully considered in retirement feasibility projections. From a purely financial perspective, these increased spending levels early in retirement are typically offset by reduced spending in later years.

Without question, a comprehensive financial plan and retirement feasibility study should be undertaken by any person considering retirement. Each situation is different, and the correct course of action can vary wildly by individual. Some potential land mines, however, are universally applicable to all retirees.

[1]https://www.fidelity.com/viewpoints/personal-finance/plan-for-rising-health-care-costs

[2]https://www.kitces.com/blog/age-banding-by-basu-to-model-retirement-spending-needs-by-category/

Sources:
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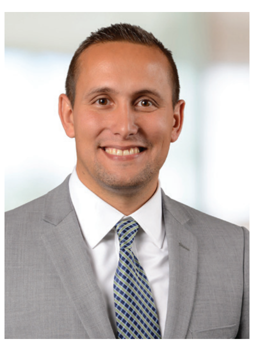

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Tom Taranto has been with HBKS® since 2011. He has extensive experience working with high-net-worth families on comprehensive financial planning, estate planning, insurance planning and asset management services. He has worked with a wide array of clients, including institutional investors, major donors, small businesses and non-profit organizations. He specializes in finding solutions for business and land owners seeking unique financial planning. Specifically, he has helped many clients capitalize on oil, gas and other energy-related investments in order to maximize the yield of their ventures.

Tom earned his B.S. in business administration in marketing and logistics from The Ohio State University's Fisher College of Business and M.A. in higher education administration, also from The Ohio State University. He is a CERTIFIED FINANCIAL PLANNER™ and an Accredited Investment Fiduciary®.