



Everything Jersey

For Monmouth County couple, cash flow looks good, but extra insurance may come in handy

By Karin Price Mueller/The Star-Ledger

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Mina, 61, is retired and already collecting her pension. Her husband Jerry, 62, is almost there. They're not sure how to determine which of Jerry's pension options would be the best for their financial future.

"Our biggest concerns are having enough cash flow from pensions and Social Security to live on, and not having to withdraw money on a regular basis from retirement savings until required to do so at age 70½," says Jerry.

The couple, whose names have been changed, have saved \$177,600 in Jerry's employer-sponsored retirement plan, \$293,840 in IRAs and \$500 in a checking account. Jerry's pension is expected to be in the \$43,000 range, and he'll receive \$21,120 in Social Security in 2011. Mina's Social Security of \$17,424 would begin in 2011.

The Star-Ledger asked Andrew Novick, a certified financial planner with Condor Capital Management in Martinsville, to help Jerry and Mina analyze their retirement income options.

THE SITUATION

Jerry, 62, is just about ready to retire, joining his wife Mina, 61, who already has stopped working. The couple wants to make sure they choose the right pension payout option for Jerry, to make sure they have enough income for their retirement years. They don't want to tap their investments for retirement income until they absolutely have to.

NET WORTH

ASSETS

Checking: \$500

IRAs: \$293,840

457 Plan: \$177,600

Home: \$460,000

Personal Property: \$10,000

Autos: \$35,000

Total assets: \$976,940

LIABILITIES

Mortgage: \$180,000

Home-equity loan: \$725

Car lease: \$9,452

Total liabilities: \$190,177

Total net worth: \$786,763

BUDGET

ANNUAL INCOME

Jerry: \$104,880

Mina Pension: \$44,000

MONTHLY EXPENSES

Income taxes: \$1,371

Housing \$2,031

Home-equity loan: \$100

Utilities: \$554

Food: \$1,170

Personal care: \$300

Transportation: \$658

Medical: \$450

Entertainment: \$35

Vacations: \$250

Gifts: \$175

Charity: \$125

Misc.: \$1,200

THE WAY OUT

The Monmouth County couple could do just fine with several pension payout options as long as they make sure to purchase additional term life insurance on Jerry's life, which would give Mina cash equal to Jerry's lost pension should he die first. The couple should stay aware of taxes as they start to tap their savings in retirement.

View the couple's retirement projections.

"It seems that most of their living expenses will be covered by their pensions and Social Security so they will not need to dip into their portfolio except for extraordinary items," Novick says.

After running some numbers, Novick says the results indicate their investment portfolio, combined with their pensions and Social Security benefits, will likely be able to provide a maximum gross annual income of \$129,367 in today's dollars during retirement, up to age 100.

He recommends spending less than the maximum because some income taxes will have to be paid out from that annual amount. Assuming a combined average federal/state tax rate of 20 percent on the entire maximum recommended amount, they'd be left with their estimated \$87,600 living expenses, so they should have a comfortable cushion, he said.

Jerry has several pension payout options. The option with the highest payout is the single life pension benefit, which would pay \$43,225 a year.

"The risk of taking a single life version is the loss of all pension benefits at Jerry's death," Novick says. "This is a significant financial risk for Mina."

The risk, though, could be mitigated with life insurance on Jerry to cover the present value of his pension benefits, Novick says. With a single life payout of \$43,225, a 23-year life expectancy, and a 5 percent interest rate, he estimates the present value of Jerry's pension at nearly \$600,000. That means Jerry would have to increase his current life insurance.

Novick says another alternative is a pension payout option that includes a survivor benefit. For Jerry, a 100 percent survivor benefit option would reduce his pension income by nearly \$7,000 a year, to \$36,310 a year.

"Not only is this reduction more than the estimated cost of securing reasonable life insurance coverage (depending on his health), it also provides no protection to the heirs in the event both spouses die before receiving the full value of the pension," Novick says.

But taking this option, along with securing some life insurance, such as the \$250,000 15-year term policy Jerry is already in the process of securing, seems like a reasonable approach.

Another possibility, Novick says, is to take yet another option, which pays \$41,409 a year with a \$397,667 declining death benefit payout.

"The combination of the declining death benefit and the \$250,000 15-year policy will provide nice protection to both the spouse and the heirs and does not result in such a severe reduction to Jerry's pension income," Novick says. As such, this is the pension option that we used in the retirement projections."

Jerry and Mina describe themselves as conservative investors, as is evidenced by their 35 percent equity and 65 percent fixed income asset allocation.

"This type of allocation emphasizes income and capital preservative, but offers enough growth opportunity to keep ahead of inflation," Novick says. "Moreover, this allocation also seems appropriate in their retirement years."

In general, Novick likes mutual funds and exchange-traded funds (ETFs), calling them excellent, low-cost investment vehicles that can provide broad diversification across multiple investment styles.

He recommends investors have exposure to equity funds that have a "growth" bias, a "value" bias, some that track a passive index (such as the S&P 500) and some that provide exposure to the international and small company areas. Similarly, for bond funds, investors should look for funds that give them a broad exposure to different areas of the bond market, such as government, corporate and municipal bonds, he said.

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