



Retirement-ready Morris County couple should reallocate assets

By Karin Price Mueller/The Star-Ledger

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Bill and Roz are heading for retirement a little sooner than planned. Bill, 57, receives a pension from his old employer, but he also brings in some consulting income. Roz, 51, lost her job and she's not confident that she'll find a new one.

"Can we maintain our lifestyle on Bill's pension and consulting income, or do one or both of us need to go back to work full time?" says Roz. The couple hopes that in five years neither of them will have to work and they'll downsize their home to a smaller one in a cheaper area.

Bill and Roz, whose names have been changed, have set aside \$251,737 in 401(k) plans, \$306,576 in IRAs, \$44,525 in mutual funds, \$20,013 in a brokerage account, \$19,000 in bonds, \$10,091 in Certificates of Deposit, \$88,140 in money markets, \$25,967 in savings and \$300 in checking.

The Star-Ledger asked Andrew Novick, a certified financial planner with Condor Capital in Martinsville, to help Bill and Roz assess their retirement readiness.

The situation

Bill, 57, recently retired, and Roz, 51, may face retirement herself. She lost her job and has been unable to find another. The Morris County couple wants to know if they can afford to live on Bill's pension and consulting income until Social Security kicks in. They're also wondering if they should pay off their home equity loan.

The way out

If the couple can keep expenses in check, they can afford to officially start retirement now. They should reallocate their assets for a more diversified and more conservative portfolio, and they'd be smart to hold on to their cash, just in case, instead of paying off their home equity loan.

Boosting exposure

The bulk of Bill's and Roz's investments are in mutual funds, and most are relatively low-cost funds. But certified financial planner Andrew Novick says they should **boost exposure to small company and international**, and consider dedicating a small percentage to commodities and/or real estate. Additionally, Novick recommends they consider some funds that invest in Treasury Inflation-Protected Securities, high-yield bonds and international bonds to expand diversification on the fixed income side. Bill and Roz consider themselves moderate investors, so their current 55 percent equity and 45 percent fixed income allocation seems appropriate, he says. But given that they're not really working now, Novick says they should consider going more conservative: 40 percent equities and 60 percent fixed income.

Net worth

ASSETS

Checking: \$300

Savings: \$25,967

Money market: \$88,140
CDs: \$10,091
Bonds: \$19,000
IRAs: \$306,576
401(k): \$251,737
Brokerage account: \$20,013
Mutual funds: \$44,525
Home: \$475,000
Personal property: \$40,000
Autos: \$35,000
Total assets: \$1,316,349

LIABILITIES

Home equity loan: \$56,820
Total liabilities: \$56,820
Total net worth: \$1,259,529

Budget

ANNUAL INCOME

Bill's Pension Income: \$41,300; Bill's Consulting Income: \$15,000

MONTHLY EXPENSES

Income taxes: \$2,927
Housing: \$2,895
Utilities: \$645
Food: \$400
Personal care: \$180
Transportation: \$525
Medical: \$50
Entertainment: \$70
Vacations: \$250
Gifts: \$175
Charity: \$25
Pet care: \$25
Misc.: \$200

"It seems they are relatively good shape even if they have underestimated their living expense," Novick says. "Nonetheless, considering their young age, I encourage them to continue looking for work now to delay tapping the portfolio for income — at least until their Social Security benefits start at age 62."

Novick ran some numbers to examine the couple's retirement outlook. He made some assumptions for the calculations, including a 6 percent annual return on investments, a 3 percent inflation rate, that the couple would each take Social Security at age 62 and that they'd downsize their home in five years.

The projections indicate a maximum retirement income of slightly more than \$98,000, Novick says, including Bill's pension, Social Security at age 62 and portfolio withdrawals.

"I recommend spending less than the maximum since some income taxes will have to be paid out of this amount," Novick says.

Because the majority of their portfolio consists of tax-deferred accounts and withdrawals out of these accounts are taxable, taxes are an important consideration, Novick says. Assuming an average tax rate of 20 percent reduces their spendable retirement income to about \$78,000.

"This is still in excess of their estimated living expenses of \$72,000 per year," he says. "Plus, their home equity loan will be paid off in a few years, reducing their living expenses down to just \$57,000, and their living expenses are likely to decline once they downsize their home in a few years."

Novick also took a look at the couple's life insurance. Bill has \$250,000 of term insurance and Roz has \$500,000 of term. Novick says he views life insurance predominantly as an income replacement tool, but he says when you retire, you no longer generate income, so your need for insurance is significantly reduced.

The couple doesn't need life insurance as income replacement — they could survive without each other's Social Security and Bill's pension will continue to pay Roz for her lifetime if Bill dies first. Novick says they may want to consider term policies, however, to replace the value of Bill's pension as an inheritance, as their heirs will never receive a penny from the pension itself.

Novick says, considering their net worth, Bill and Roz seem like good candidates for long-term care insurance to cover nursing home or home health costs.

"While I feel that they are a little young to consider LTC, it will be much more affordable if they secure a policy now," Novick says.

He recommends they consider a policy with at least a five-year benefit period, preferably a lifetime benefit. They'd need at least a \$150 daily benefit, and a \$200 daily benefit is preferable. Novick says they should select a policy with at least a 3 percent compound inflation adjustment. The combined premium for this type of policy will cost between \$3,000 and \$5,000 per year depending on the specific benefits.

With such a high cash reserve, Novick says he'd normally recommend Bill and Roz pay off their home equity loan. This would reduce their living expenses immediately and the tax benefit they're receiving is quite small.

"However, considering that their employment situation is in a state of flux — Bill just retired and may or may not pursue consulting work combined with the fact that Roz is unemployed and may or may not find another job — keeping a high cash reserve and paying the loan off slowly seems prudent," Novick says.

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