As America ages, clients are demanding more retirement income planning products and services, and planners are stepping up to meet that demand. Whether a planner's primary strategy for providing retirement income involves a systematic withdrawal, time-based segmentation, essential versus discretionary income, Social Security and pensions, or a combination of strategies, planners are generally successful at executing retirement income planning. They’re keeping the majority of their clients in or near retirement from having to make any significant changes to their retirement plans or lifestyles, notwithstanding a lagging economy.

According to FPA’s 2010 Financial Adviser Retirement Planning Experiences, Strategies, and Recommendations Study, which queried 425 FPA members in September, 60 percent of planners’ clients received retirement income products, services, or advice from them in the last 12 months, compared to 53 percent of planners’ clients in 2009, according to similar research conducted last year.1

The increase in retirement income planning may simply be attributed to the fact that each year more baby boomers are closer to retirement. However, it may also be thanks to a shift in attitude. “At the end of 2008 and early 2009, we saw a lot of people who were just too shell shocked to do anything,” says Michael E. Kitces, CFP®, CLU, ChFC, director of research at Pinnacle Advisory Group. He indicated that people are re-emerging from their shells, engaging planners, and seeking solutions, which would help account for the reported increase in retirement income planning.

Success Across All Strategies
In 2010, planners report that 60 percent of their clients in or near retirement have made no significant changes to their retirement plans; this is the same finding as the 2009 survey.

The 2010 survey also shows that just 17 percent of planners’ clients in or near retirement have had to delay their retirement date. This is significantly less than what has recently been reported in two consumer polls. A survey from consulting firm Towers Watson shows that 40 percent of U.S. workers plan to delay their retirement,2 and similar research from Sun Life Financial shows 52 percent of U.S. workers expect to work at least three years longer than originally planned.3

Rebecca King, manager of the FPA Research Center, says FPA’s 2010 retirement study continues to affirm the value of financial planning.

“We’ve seen this type of success in other research as well, such as the 2008 Value of Financial Planning study, so we know that professional financial planning provides tangible benefits,” says King. “The 2010 research shows that financial planning provides benefits in times of economic crisis as well as economic growth.”

According to the 2010 survey, all retirement income strategies generate approximately the same level of success when measured by the financial and lifestyle changes clients in or near retirement have to make. (See Table 1 for details on the strategies.) However, the essential versus discretionary income strategy does correspond to a higher percentage of clients who have had to significantly adjust their lifestyles than all other strategies (read more about this on page 31).

As shown in Table 2, planners use a variety of products for retirement income planning purposes. Overall, planners are successfully helping clients in or near retirement maintain their lifestyle and retirement plans no matter which products they most often use. However, planners who are not making any product recommendations have the highest percentage of clients who have had to significantly adjust their lifestyle due to economic conditions.

“Planners who are not making any recommendations should take a close look...
at the percentage of clients who are implementing the retirement plan,” says King. “It’s possible that their clients simply aren’t getting these recommendations anywhere and, as a result, are not effectively saving or planning for retirement.”

**Essential Versus Discretionary Income**

The 2010 study data show that among planners who primarily use an essential versus discretionary income approach, an average of 25 percent of their clients in or near retirement have had to significantly adjust their lifestyle in 2010—the highest percentage of any income strategy used.

This does not necessarily mean that the essential versus discretionary income approach is the least effective strategy for keeping retired clients on track; instead, it may point to the planner’s ability to better identify when clients need to make changes.

For Jonathan T. Guyton, CFP®, principal of Cornerstone Wealth Advisors and author of influential research on safe withdrawal rates, the survey finding related to essential versus discretionary income may be a product of recency bias. Recency bias is the phenomenon of giving more weight to recent events than events that took place in the past.

He offers this example: A retired client with a $1 million retirement nest egg has $30,000 in essential expenses. Using the essential versus discretionary income approach, you may be interested in buying an annuity to guarantee $30,000 of inflation-adjusted income, and you may need as much as $800,000 or more of that $1 million to do so. Because the essential income is locked down in “safe” things, you may be inclined to invest the remaining $200,000 of discretionary funds more heavily—say 75 to 80 percent—in equities.

“Then you get a big downturn in 2008 and 2009, and most of that $200,000 is in equities, so now you’re down to around $140,000 or $150,000, and

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**Table 1: Income Distribution Strategies Used**

Which one of the following best describes the strategy you use most frequently to provide retirement income to your clients?

<table>
<thead>
<tr>
<th>Strategy</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Structured systematic withdrawal program:</strong> Diversify investments based on client’s risk profile and manage the total return of the client’s entire portfolio. To provide income, draw down a percentage of the portfolio periodically or withdraw interest and dividends only.</td>
<td>40%</td>
<td>50%</td>
</tr>
<tr>
<td><strong>Time-based segmentation approach:</strong> Set up separate pools of investments with lowest-risk investments in the near-term time horizon segment, somewhat higher-risk investments in the next segment, and riskiest portfolio in the longest-term segment. Income is drawn from one segment at a time. Once the first segment is depleted, assets from the second segment are used for income.</td>
<td>32%</td>
<td>28%</td>
</tr>
<tr>
<td><strong>Essential versus discretionary income approach:</strong> Classify client’s retirement expenses as essential or discretionary. Low-risk investments or annuity guarantees are selected to fund the essential expenses. A mix of medium- and higher-risk investments is selected to fund the discretionary expenses. Income is drawn from both funds: one fund to cover essential expenses; the other fund for discretionary spending.</td>
<td>14%</td>
<td>14%</td>
</tr>
<tr>
<td><strong>Social Security and/or pension:</strong> In most cases, do not use a structured portfolio or strategy to provide retirement income to clients. Clients mainly live on pensions and Social Security, which may be supplemented periodically.</td>
<td>7%</td>
<td>4%</td>
</tr>
<tr>
<td>Other (please specify)*</td>
<td>6%</td>
<td>5%</td>
</tr>
</tbody>
</table>

*Other includes a combination of the above strategies and managed cash flow. Source: FPA’s 2010 Financial Adviser Retirement Planning Experiences, Strategies, and Recommendations Study

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**Table 2: Financial Products Used**

Which of the following financial products do you use/recommend with your clients for retirement income planning purposes? (Select all that apply.)

<table>
<thead>
<tr>
<th>Options</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income and dividend-paying investments</td>
<td>86.60%</td>
</tr>
<tr>
<td>Bonds</td>
<td>71.10%</td>
</tr>
<tr>
<td>Long-term care insurance</td>
<td>67.50%</td>
</tr>
<tr>
<td>Treasuries/TIPS</td>
<td>54.60%</td>
</tr>
<tr>
<td>Exchange-traded funds (ETFs)</td>
<td>54.40%</td>
</tr>
<tr>
<td>Certificates of deposit (CDs)</td>
<td>52.40%</td>
</tr>
<tr>
<td>Single premium immediate annuities (SPIAs)</td>
<td>43.10%</td>
</tr>
<tr>
<td>Variable annuities with guaranteed living benefits (GMIBs, GMABs, GMWBs)</td>
<td>43.10%</td>
</tr>
<tr>
<td>Medi-gap insurance</td>
<td>33.12%</td>
</tr>
<tr>
<td>Fixed deferred annuities</td>
<td>25.90%</td>
</tr>
<tr>
<td>Reverse mortgages</td>
<td>16.00%</td>
</tr>
<tr>
<td>Other (please specify)*</td>
<td>10.60%</td>
</tr>
<tr>
<td>Target maturity funds</td>
<td>10.20%</td>
</tr>
<tr>
<td>Other variable annuities</td>
<td>9.40%</td>
</tr>
<tr>
<td>Other immediate annuities</td>
<td>8.20%</td>
</tr>
<tr>
<td>Long-term care annuities</td>
<td>5.40%</td>
</tr>
<tr>
<td>Managed payout funds (income replacement funds)</td>
<td>0.90%</td>
</tr>
</tbody>
</table>

*Other includes mutual funds, REITs, structured products, life insurance and limited partnerships. Source: FPA’s 2010 Financial Adviser Retirement Planning Experiences, Strategies, and Recommendations Study
The Business Benefits of Retirement Planning

Planners attribute some new client acquisition to the fact that they provide retirement planning services, and that amount of new business is growing.

In FPA’s 2010 Financial Adviser Retirement Planning Experiences, Strategies, and Recommendations Study, nearly 25 percent of planners indicate that more than 10 new clients had come to them for retirement planning services in the past 12 months, up from 17 percent in 2009.

Planners who have retirement income planning expertise are also consolidating more assets from current clients. In the 2010 study, planners indicate that 60 percent of clients who have received retirement income products, services, or advice from them have since consolidated more assets with their firm; that’s up from the 48 percent of clients who consolidated more assets in 2009.

“I think advisers are starting to realize that if they don’t take an offensive position in terms of retirement income management and planning, they are at risk of losing those clients,” says Kevin S. Seibert, CFP®, CRC®, CEBS, principal at InFRE Retirement Resource Center. “We know from research that clients have a higher probability of changing advisers 5 to 10 years prior to retirement. If they’re not confident that their current adviser is the one who can do retirement income planning for them, they will find someone who can.”

The average rate was 4.4 percent. In 2010, the average rate is 4.75 percent.

Kitces admits that it’s difficult to know what the source of that increase is, but he says it could be a result of the growing body of knowledge indicating that a 4.0 percent withdrawal rate with no other adjustments may be too low.

“I think it recognizes a growing base of research that says that for some clients, in some situations, taking a higher rate than a flat 4 percent is okay,” says Kitces.

Guyton agrees, saying planners have become more familiar with research by Kitces suggesting that in a lower market valuation environment, the withdrawal rate that is sustainable is higher; the converse is also true. Planners may also be more familiar with research Guyton has conducted suggesting that if clients are willing to make some small adjustments, then the safe withdrawal rate can be about a full percentage point higher than if they are not willing to be flexible.

But if planners are increasing withdrawal rates because they feel things are better in 2010 than they were in 2008 or early 2009, that’s counter-intuitive to what the research shows, according to Guyton.

“It may be tempting to think that when the market is at an all-time high maybe you can take out 6 percent or more, and if it’s really low you should only take 4 percent—but that is a 180-degree difference from what the research demonstrates,” he says. “In a way, though, that’s what human behavior suggests. In fact, even though the withdrawal amount may be slightly reduced in extreme down markets, the safe withdrawal percentage could actually be higher.”

Guyton offers this example: A client with $1 million is doing a systematic withdrawal, taking out $50,000 a year, or 5 percent. The market drops dramatically, and the $1 million goes to $700,000, so you tell the client he should reduce what he’s taking by 10 percent ($50,000 becomes $45,000). Now you have $45,000 of $700,000, which is about 6.4 percent.

“Your withdrawal rate has gone up and your withdrawal amount has gone down, and that flexibility, that small reduction, is exactly what you should have done in a market that is very lowly valued,” he says.

Carly Schulaka is a managing editor at FPA. Contact her at Carly.Schulaka@FPAnet.org.

Endnotes

2. Towers Watson study of 9,100 employees conducted in May and June 2010: towerswatson.com/press/2919.
Using a Hierarchy of Funds to Reach Client Goals

by Jason K. Branning, CFP®, and M. Ray Grubbs, Ph.D.

The financial planning and investment industries use a common mental map, a framework that serves to focus, simplify, and constrain thinking and recommendations. This framework, modern portfolio theory,1 is deeply embedded in the psyche of financial advisers and is applied to institutions as well as individuals, including individuals at or near retirement.

Modern portfolio theory has drawn investors into markets by touting historical long-term average stock returns. This perspective (long-term averages, law of large numbers) may best apply on a group basis—for pension funds, insurance pools, etc.—where there is an institutional time horizon of 40 years or more. Personal finance is not institutional finance; therefore, we believe that there is an alternative mental map that changes the way advisers and individuals think about the unique questions retirees must answer, and offers a hierarchy of funds to reach client goals in any market. We call this alternative mental map modern retirement theory (MRT).2

MRT suggests that historical long-term averages may not apply in individual client scenarios and seeks to offer a sustainable benefit to individuals. It proposes a perspective on retirement planning that seeks to meet the individual client’s retirement goals under any market condition or life event. The model recognizes potential limits in asset growth in good markets, but seeks to use retirement sheet assets3 versus portfolio assets. The theory defines success as a sustainable lifestyle throughout retirement.

MRT is the comprehensive alternative mental map within which modern portfolio theory fits.

Institutions Versus Individual Retirees

To understand why applying modern portfolio theory and its historical long-term averages may be misapplied to individual clients, consider the differences between institutional and personal finance.

Institutional finance deals with the ways large organizations, such as banks or insurance companies, manage risk, cash flows, business cycles, and market cycles. Corporations were created in part for perpetuity. While dependent on people to run a business, management teams can change over time and allow the business to continue. Corporations do not worry about longevity, only sustainability. Institutions never physically get sick and die. A corporation may be financially “sick,” but “death” typically looks like a corporate restructured bankruptcy, government take-over, or merger.

Inherent in an institution’s approach to investing is the entity’s substantially long (that is, more than 40 years) time horizon. This offers the institution the ability to weather market volatility, including a lost decade. Institutions do not need to manage for the decumulation of a finite asset base over short periods of 20 to 30 years. Additionally, in tough economic or business cycles, some organizations such as banks or insurance companies can diversify revenue streams or increase fees to help sustainability.

Personal finance, as defined by modern retirement theory, is the way individuals manage two risks: (1) longevity and (2) conditions within longevity. Individuals must manage
their retirement assets based on an unknowable but finite lifespan. Retirees need enough income to maintain their at-retirement lifestyle without running out of money. Additionally, retirees must be prepared to handle the conditions within longevity. These conditions include managing cash flows through a predictable decumulation of assets for life, healthcare costs or issues, a planned retirement date, monetary family obligations, a changing legislative environment for estates, and market cycles.

Rather than constructing a plan that is primarily dependent on performance of a portfolio and a safe withdrawal rate, every retiree must face up to and plan for the unknowable questions of longevity and conditions within longevity.

Using Modern Retirement Theory for the Retiree

The MRT standard is that individual retirement goals are absolute and therefore must result in a sustainable lifestyle throughout the retirement phase. To this end, MRT seeks to employ strategies that meet the client’s stated objectives in any market climate, mitigate transfer longevity risk and conditions within longevity risk, are tax efficient, and maximize assets by disbursing the client’s retirement sheet assets into four broad categories. Listed in order of priority, these four categories, or funds, are: base fund, contingency fund, discretionary fund, and legacy fund.

**Base Fund.** The core philosophy of this fund is to provide guaranteed income that can be produced in good market conditions or poor market conditions. Base income should be characterized as secure, stable, and sustainable. This income should also adjust for inflation over time and remain in place for a surviving partner. Social Security is viewed as a portion of this guaranteed base. Base income is defined as $B = B_1 + B_2$ where $B_1$ is Social Security and $B_2$ is other income-producing assets.

**Contingency Fund.** This fund offers a hedge against the unpredictable yet highly consequential events (black swans) that may occur from a personal medical issue, changes in estate laws, or with markets. Laws related to the types of events covered in this fund may change over time, so individuals should seek a legal review of their documents every three to five years. Not only do estate laws change, but there is the potential for estate taxes to be due in a negative market cycle.

**Discretionary Fund.** After lifetime income is secure and catastrophic scenarios mitigated, a flexible income fund can be established.

**Legacy Fund.** The final MRT set-aside is the legacy fund. These assets are intended to be used for inheritance or charitable purposes and will not be used to satisfy any of the prior-mentioned funds. Therefore, this fund may be more aggressively invested and may avoid inclusion in the estate through attorney-recommended trusts.

**Conclusion**

The recent decade has challenged advisers, the investment industry, and retirees in unexpected ways. Advisers have felt the tension between encouraging the client to ride out market storms in the hopes of achieving long-term market averages and fighting retirees’ negative emotions and declining portfolios. The most significant challenge has come to the individual retirees themselves, whose investment portfolios have been severely tested and for most of whom the historical averages have not been realized. These retirees are left feeling as though they have descended into a financial purgatory.

<table>
<thead>
<tr>
<th>Table 1: Institutional vs. Personal Finance</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Characteristic</strong></td>
</tr>
<tr>
<td>Entity</td>
</tr>
<tr>
<td>Time horizon</td>
</tr>
<tr>
<td>Conditions</td>
</tr>
<tr>
<td>Decumulation strategies</td>
</tr>
<tr>
<td>Taxes</td>
</tr>
<tr>
<td>Outcomes</td>
</tr>
<tr>
<td>Income</td>
</tr>
</tbody>
</table>

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Advisers must attempt to offer alternatives that reform, reframe, and reshape the context of retirement thinking. Alternatives may strive to more effectively manage or avert dangerous declines in asset value that leave retirees with the undesirable choices of work longer, increase savings, or die early. Planners should be ready to chart a new course for retirees while taking advantage of modern portfolio theory.

In “Spending Retirement on Planet Vulcan,” Moshe Milevsky, Ph.D., says, “Many of the popular products used and strategies employed by individuals in their portfolios are at odds with financial economics.” A new course should be in harmony with financial economics and offer a comprehensive approach to the goals of an individual retiree. That new course is modern retirement theory.

M. Ray Grubbs, Ph.D., is a professor of management at the Else School of Management at Millsaps College in Jackson, Mississippi. He consults with numerous private, public, and nonprofit organizations.

**Endnotes**


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**Table 2: Modern Retirement Theory’s Hierarchy of Funds**

<table>
<thead>
<tr>
<th>Funding Priority</th>
<th>Fund</th>
<th>Purpose</th>
<th>Time Horizon for Portfolio Assets</th>
<th>Possible Tools</th>
<th>Potential Hazards that Must Be Managed</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Base Fund</td>
<td>To provide guaranteed income in good or poor market conditions with investing options that extend some form of protection and are not subject to market risk</td>
<td>Immediate</td>
<td>Social Security, laddered CD interest, laddered fixed annuity income, variable annuities with guaranteed income, defined benefit pension plans, reverse mortgages, TIPS (alternative income may be generated from income-producing real estate assets or raw land, such as timber and hunting leases)</td>
<td>Primarily inflation and credit risk; using non-qualified assets prior to consuming qualified assets is preferred for tax efficiency, institutional exposure (FDIC or SIPC, or State Guarantee Association)</td>
</tr>
<tr>
<td>2</td>
<td>Contingency Fund</td>
<td>To mitigate and transfer risk to maintain a sustainable retirement lifestyle by having assets that are available on short notice and that will not suffer market loss even in negative market cycles</td>
<td>Immediate to 1 year</td>
<td>Short-term FDIC structured notes, laddered CDs, life insurance for estate planning, market neutral or inverse funds, cash</td>
<td>Primarily an issue of risk acceptance, mitigation, or transference. Medical risks may be mitigated with Medicare along with an appropriate medical supplement; a long-term care event may be mitigated with long-term care insurance (preferably purchased before age 60) or buying into a continuing care facility as an independent resident</td>
</tr>
<tr>
<td>3</td>
<td>Discretionary Fund</td>
<td>To handle travel expenses, auto purchases, and other events that are flexible in need or occurrence</td>
<td>2 to 10 years</td>
<td>Laddered CDs, laddered FDIC-insured structured notes, cash value from life insurance, and TIPS on the more conservative end; a more moderate approach would use a conservative investment portfolio or dividend-paying preferred stocks</td>
<td>Inflation, institutional exposure (FDIC or SIPC, or State Guarantee Association)</td>
</tr>
<tr>
<td>4</td>
<td>Legacy Fund</td>
<td>To be used for inheritance or charitable purposes</td>
<td>&gt; 10 years</td>
<td>Charitable trusts (e.g., CRAT, CLUT), donor-advised funds, a diversified stock and bond portfolio, whole or permanent life insurance, life insurance trusts</td>
<td>Changes in estate tax laws</td>
</tr>
</tbody>
</table>
Successful retirement planning and retirement distribution planning not only require smart portfolio management and efficient withdrawal strategies but also the right conversations with clients. Asking clients when they want to retire should not be part of that conversation, according to financial life planning expert Roy Diliberto, CFP®, ChFC. And even assuming clients will retire at all can be a fatal flaw.

The Journal recently caught up with Diliberto, former FPA president who currently serves as chairman and CEO of RTD Financial Advisors, to talk about the life planning aspects of successful retirement planning.

FPA: How, as a planner, can you best help your clients shift their mindset from “How much money do I need to retire?” to “What kind of life do I want in retirement?”

DILIBERTO: This is going to sound overly simplistic, but ask them that question. Ask them about the kind of life they want before you ask them about how much money they need. Money’s the servant, not the master. You don’t live a lifestyle based on the amount of money you have. You live a lifestyle that you’d like and then see if you can get enough money to do it. And if you don’t, maybe it takes waiting a year or two to do that.

The reality is you have to ask people these questions. A lot of people retire from things as opposed to to things. And I think it’s extremely important that you retire to something as opposed to from something. And we have that conversation with people who are approaching retirement on a regular basis. We ask them about what kind of a life that’s going to be, what they are going to do, what their plans are. And then sometimes people just say, “We might want to rethink this,” because they feel they may have nothing to go to that’s satisfying.

We had one client who told me she was ready to retire. She had us run the numbers and so forth, and she told me she was ready to go. In six months or a year, she was going to do it. Then she had a minor medical setback and was forced to be home for a period of time. And then when she finally came back and said, “If that’s what retirement is going to be like, I want no part of it.” So, you have to make sure that you’re doing something that’s going to be satisfying to you—whatever that may be—and fulfilling in your life.

If you want to discuss those things, you’ve got to ask the questions, and maybe some people are reluctant to do that. Some planners think that’s none of their business, that all they need to do is talk about the money. I don’t find that works.

FPA: What happens when what clients say about their retirement goals doesn’t line up with the actions they take? Can a planner help clients identify some core values?

DILIBERTO: It’s an interesting question. We can’t approach this as if this is the first time you’re ever having a conversation with this person. So you’ve got to approach it based on everything you’ve learned about this client over the years. In the initial meetings process, we ask clients questions about themselves, about their history, and how they grew up. We need to understand their values and what’s most important to them in their lives so we have a pretty good idea about what really matters to them.

For example, there are people who retire who say they want to travel, and they never travel. There’s only so much you can do, obviously, but it’s a question of just reminding them of the things that they said were important, and if they’re not doing those things to keep reminding them, “This is something that you said was important to you. Is there any reason you don’t want to do it?”

Now, interestingly enough, many times the reason is because they’re not earning money anymore and they’re afraid. They’re afraid to spend their money, even though the projections...
indicate that they have more than enough. And you could try to convince them that they are in no danger of running out of money, but since it is an emotional issue, showing them the numbers may not have any effect on their behavior. You’ve got to go back to the emotions and the things you’ve discovered and have those conversations about why they’re acting the way they are and are not spending the money that they had intended to spend.

**FPA:** Many planners ask clients, “When do you plan to retire?” Is there anything wrong with asking that question?

**Diliberto:** I hate that question. It’s a presumptuous question. We ask, “How do you visualize your life in your 60s, 70s, 80s, and beyond?” not, “When do you want to retire?” I would assume that someone like Justice Stevens was asked that question 100 times and he probably got angry every time he was asked.

**FPA:** In your book *Financial Planning: The Next Step*, you write about the importance of avoiding assumptions. What are some common assumptions planners make when it comes to retirement planning?

**Diliberto:** I think the most egregious assumption is that everybody retires. Since people are asked the question, “When do you plan to retire?” they must think that they need to have a date. So they’ll say, “Oh, when I’m 65,” because that’s when people retire. And that’s another assumption—that most people retire when they’re 65 because that’s some magic age that somebody came up with at some point, probably when people lived to be 64.

Another assumption that people make is that their portfolios have to become very, very conservative now that they’re retired, even though they probably have a 30-year period of time to go if they do retire at 60 to 65 years old. So now they start to ratchet down the portfolio. In a way, that may not provide enough growth for them to do all the things that they want to do. That, I think, is a faulty assumption that is reinforced by the things they hear from the media.

Another assumption is you’re going to spend less money when you retire. That’s ridiculous. Most of our clients who retire spend more money the first few years they’re retired, not less. Using rules of thumb, like you need 75 percent of your income—I have no idea where that came from—I think is an assumption people make about how much money they’re going to spend.

That you’re going to be in a lower tax bracket is another assumption that people make that I think is erroneous. When those distributions start, their tax bracket may go higher than it ever was in their life for all we know.

**FPA:** If a couple has significantly different images of what their retirement lifestyle should look like, how can a planner help get them on the same course?

**Diliberto:** It’s very difficult. You have to make sure that each client is communicating to each other. And I help facilitate that by asking each spouse questions so that they understand what each other may desire. However, we may be limited in what we can do as planners, and if there are significant differences, they may need some help that planners aren’t qualified to give.

**FPA:** Is there anything else you want to say about using life planning to help clients plan for retirement?

**Diliberto:** Ask those questions that are relevant about the person’s life and continue to ask those questions at annual meetings. In our firm, we have an annual renewal meeting (thanks to Elizabeth Jetton), and we don’t call it a review meeting for a very good reason. A review meeting perhaps only looks at numbers. Our renewal meeting is about renewing your goals and your life and revisiting what is important to you.
One of the biggest decisions advisers face in developing retirement income strategies for their clients is when the clients should begin collecting Social Security benefits. For couples, the decisions—and options—can be particularly complex if they are able to delay taking their benefits. This article focuses on five Social Security strategies that you can use with your clients.

Identifying optimal Social Security strategies can help clients maintain their quality of life and may result in a significant increase in benefits collected over their lifetimes. But first, let's briefly look at the basic factors to consider when deciding when your clients should begin collecting Social Security benefits, including their income needs, ages, health, other income sources, desires to work during retirement, and marital status.

Factors to Consider

Determining needs. The first step should be to figure out how much income clients will need in retirement and where this money will come from. Social Security usually provides at least 20 percent of pre-retirement income. The Social Security Administration's (SSA) online retirement estimator at www.socialsecurity.gov/estimator can help you project client benefits based on their earnings record and the age at which they plan to begin taking payments. [Editor's note: FPA also offers a consumer-oriented Social Security predictor tool that offers an idea for how Social Security will be affected by various legislative proposals at www.FPAnet.org/SocialSecurityPredictor/ScenarioSelection.aspx.]

Setting a retirement date. When your clients want to retire and whether they want to keep working for income in some capacity during retirement are, of course, key questions. This decision may hinge on the value of their other financial resources, whether they have health issues, and perhaps even their expected longevity. If they leave their jobs before age 62, what will they do for income before they are eligible for Social Security? If they are under age 65, what will they do for medical insurance before qualifying for Medicare? Taking a part-time job can help fill income gaps and cover health insurance premiums and may enable them to delay applying for Social Security for some time.

Value of waiting. Clients can certainly begin drawing their Social Security benefits at age 62, but there is no requirement to do so and the benefits of waiting can be significant: approximately an 8 percent annual increase in benefits in real (inflation-adjusted) terms for every year they delay taking benefits from ages 62 to 70. That means that if clients delay drawing benefits from 62 to their full retirement age (FRA)—66 for most boomers—theyir monthly checks could be more than 32 percent greater than if they didn't wait. If they wait until age 70, their checks could be 87 percent higher with compounding. Even without additional savings, many retirees would come out ahead over the long term by continuing to work for at least a year or two past 62. This is because their earnings could cover their expenses and their savings could continue to compound without withdrawals, assuming sufficient longevity to break even.

Working. Until your clients reach their FRA, the SSA will deduct $1 from their benefits for every $2 they earn above the annual wage limit, which is $14,160 in 2010. At their FRA, however, their monthly checks would be gradually increased to offset any earlier reductions due to earning more than the wage limit. Once clients reach their FRA, there is no SSA provision for a reduction in their benefits because of earnings.

Marital status. The decision about when to take benefits not only directly affects your clients but also their spouses. If they are married, this decision should be approached as a couple because when the first spouse dies, the surviving spouse is eligible to receive the larger of the deceased spouse's benefit or their own.
**Five Strategies for Couples**

The following five examples, offered for illustration only, show the financial effect of various Social Security strategies for couples. Call them Mary and John, both currently age 61. Mary earns $53,000 and John earns $84,000. And assume that John dies at age 80 and Mary dies at age 95. See Figure 1.

**Option 1: Both start Social Security at 62.** If Mary and John start taking benefits at 62, the total (pretax, inflated) benefit paid out from Social Security during John’s and Mary’s lifetimes will be about $1.24 million. Mary’s payment in the first year after John dies rises to what John would have received, increasing her annual benefit from $20,000 to about $28,000.

**Option 2: Mary starts at 62 and John waits to 70.** If John delays taking Social Security until 70, Mary will receive about $52,000 in the first year of widowhood—almost twice as much as in the previous example. The total benefit will be approximately $1.79 million, $550,000 more than if they both began drawing benefits at age 62.

**Option 3: Mary and John both wait to 70.** If they both delay taking benefits until 70, Mary again will receive approximately $52,000 in the first year after John’s death, but their total benefit will be about $1.88 million ($640,000 more than in Option 1) because Mary had been drawing her highest possible benefits as a result of delaying taking them until 70. In other words, both delaying enables this couple to receive more inflation-adjusted income later in life—a form of longevity insurance.

**Option 4: John waits to 70 and Mary starts at 62 but uses the spousal benefit.** When John attains his FRA (age 66), he files for spousal benefits. This strategy allows John, while delaying drawing his own Social Security benefit until 70, to begin receiving 50 percent of Mary’s Social Security benefit. At age 70, John reapplies to the SSA to begin receiving his own benefit, which will be considerably larger than the spousal benefit he had been receiving since 66. This strategy results in about $40,000 more in cumulative retirement income than Option 2—the same strategy without taking advantage of the spousal benefit.

**Option 5: John and Mary wait to 70 but Mary claims spousal benefit at 66.** In this example, Mary and John both delay benefits until age 70 with another twist. At his FRA, John files for his benefits but then immediately suspends the application, thereby enabling Mary (once she also reaches her FRA at 66) to claim spousal benefits based on his higher earnings. At age 70, Mary reapplies to the SSA to begin receiving her own benefits, which are higher than half of John’s. (John does not need to reapply because it happens automatically.) This is the highest yielding of the five strategies, resulting in $54,000 in additional cumulative spousal benefit income over Option 3—the same strategy without the spousal benefits. It yields almost $700,000 more than the couple would have received if they had both started taking benefits at age 62.

**Permutations and Planning**

With couples, advisers may encounter many permutations on the above scenarios, depending on the husband’s and wife’s earning history, ages, and other factors. For example, if one spouse earned less than half of the higher spouse’s benefits and therefore her spousal benefits exceed her own benefits, there is no benefit to her from delaying Social Security past her FRA.

Helping clients navigate these and other complexities offers real opportunities for advisers who are knowledgeable about Social Security benefits to significantly add to their clients’ retirement income streams.

Christine S. Fahlund, Ph.D., CFP®, is a senior financial planner and vice president at T. Rowe Price where she specializes in retirement accumulation and distribution strategies and estate planning.

**Endnotes**

1. To determine your clients’ FRA, visit www.socialsecurity.gov.
2. In the calendar year during which clients reach their FRA, the reductions in the months prior to their birth date are less than in the months in previous years.
3. The spouse earning less ($53,000) would have been eligible to receive $9,452 at age 66. By taking the spousal benefit instead, the higher-paid spouse can receive 50 percent of the lower-earning spouse’s benefit—or $9,726—each year (increased for inflation) from ages 66 through 69.