

Retirement Planning, Part 14
Converting Assets for Lifetime Income
By Gary Case

When it comes to lifetime retirement income, there are many trade-offs to be considered. A very personal trade-off is the choice that retirees must make about how much they can afford to spend in retirement. The decision depends on the full array of income sources they can draw on. Unless retirees have sufficient guaranteed pension and Social Security to cover all of their expenses for life, they will have to consider strategies for structuring and drawing down their life savings to provide income to cover those expenses not met by guaranteed income sources. Doing so will require trade-offs—sacrificing liquidity and flexibility, for example, to secure guaranteed income streams for life.

“Guaranteed” is an interesting word, since guarantees are made by governments, institutions or companies. When a guarantee is made by a government that also prints currency, we usually assume that currency will be available to pay the liability. However, government programs can change and guaranteed amounts can change. When an insurance company issues a guaranteed income stream, the ability of the company to meet its obligation is the guarantee. Even with these caveats, using guaranteed income sources to provide retirement income makes a lot of sense for most people.

Using the most predictable income sources to meet essential expenses, then converting financial assets to cover any income gaps is the first step in the process.

Reliable Income Sources

- Social Security
- Company Pension
- Income Annuities

Essential Expenses

- Food
- Clothing
- Shelter
- Health Care

Then, after there is a reasonable certainty that essentials are covered, financial assets can be directed to fund more “discretionary” expenses such as travel, entertainment and club memberships.

Meeting essential expense needs first can give retirees a sense of assurance that their most critical costs may be covered for life. As the name suggests, discretionary expenses are “nice to have,” which can be adjusted up or down depending on lifestyle changes or the performance of financial assets earmarked to cover these expenses. The assurance of knowing essential expenses are covered may better position retirees to ride out periods of volatility in the financial markets.

A good exercise would be to determine your essential expenses if you were retired today. Be sure to take into account that your home may be paid for prior to your retirement. Next time this column will address options for converting financial assets into sources of lifetime income.

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