RETIREMENT INCOME PLANNING

FROM SAVINGS TO INCOME

GET UP TO 20% OR MORE RETIREMENT INCOME WITH LESS RISK

A series of articles published on Kiplinger.com

"3 Steps Toward Building a Retirement Income Plan"

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From Savings to Income

Most investors saving for retirement have heard the advice to "diversify." They know their stock holdings should be spread among several types of companies and further split between large, small and medium firms. Bonds and other lower-risk investments should be included as well.

That's a good template for asset allocation.

Just as important as you approach or begin retirement—and not usually discussed by financial advisors—is the concept of *income allocation*.

Even a well-diversified portfolio, in the form of stocks and bonds, may not produce the cash flow from withdrawals you need when the market collapses. Income allocation significantly reduces the risk of market volatility to produce dependable income every year.

During years I have been helping people with their retirement planning, I realized that the usual guidance—rely primarily on withdrawals of savings to fund expenses when you stop working—doesn't provide enough of an answer.

In this eBook, you will learn how to use your hard-earned savings to increase your income as you minimize risk.

The result? Real peace of mind that comes from a combination of guaranteed lifetime income, bolstered by a portfolio of stocks, bonds and cash.

If that is your goal, keep reading.

– Jerry

It All Starts with Asking the Right Question

Most retirement planning asks, "How much savings?"

The right question is, "Do I have enough income to retire?"

The stock market recently gave us another reminder of what volatility feels like.

I'm writing on the day following a two-day, 8% plummet in the Dow Jones average. Everyone I talk to asked, "What happened?" "What do I do?" "Will it get worse?"

The most frantic questioners were those who had the largest amount of their savings in stocks, especially the ones who depend on equities to provide them with their retirement cash flow. (Even the Millennials got spooked when their robo-advisors jammed up.)

The pundits immediately suggested that investors "stay the course." Some also opined, "This market correction probably was a good thing."

But think about the investor whose cash flow depends on the value of the market, someone who takes required minimum distributions from her 401(k) or rollover IRA. She just experienced serious "Income Volatility"—a reduction in income from a fall in the market. It was the last thing she needed.

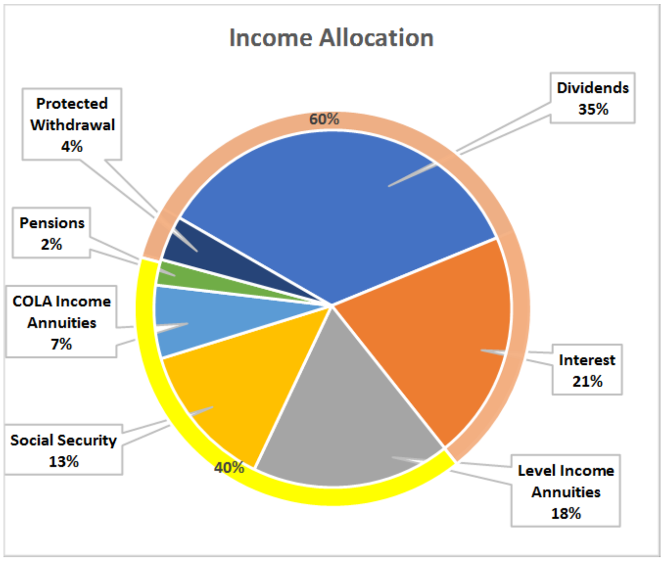
Income allocation over asset allocation

I believe we can create income allocation strategies that don't collapse with our confidence when the market goes haywire—and that can reduce income volatility to near zero.

Here is a rough illustration of my own situation, which allowed my wife and me to stay calm during the drop. I concentrate on income allocation and the minimization of income volatility, not asset allocation and market volatility. And the plan is to provide income for the rest of our lives, however long it might be.

It All Starts with Asking the Right Question

The pie chart shows where my income comes from. Note that a high percentage of this income is likely to grow, addressing most of my concerns about inflation. If you add in my life insurance, long-term care insurance and longevity insurance in the form of a deferred income annuity called a QLAC, my plan is protected from life risks. Not everyone can get to a plan like this but it's worth striving for.



How did I get to this position?

As an investment advisor, I understand the power of high-dividend stock portfolios and ways to manage income volatility.

As a retirement income planner, I understand the difference between income and withdrawals. (When your plan is set up correctly, it means that today's cash flow doesn't impact future income.)

As an actuary, I appreciate and understand the unique benefits that life insurance, long-term care insurance and income annuities can provide.

And as a fellow Boomer and consumer of financial products, I understand the peace of mind I get from regular "paychecks" – along with the pleasure of seeing as little as possible go out in taxes.

While my background gives me a particular advantage, there's one thing that all investors and their advisors can do for us Boomers: Think of the plans you're building for retirement as being not about "asset allocation," but about "income allocation." The goal is to minimize income volatility.

Income Planning Starts with Income Allocation

Do you have enough income to retire?

As a famous TV sports reporter would say, "Let's go to the videotape!" When the talking is done, it's always good to look again at the results to find out who won the race and why they won.

Unfortunately, most "experts" often view the wrong race. In the case of your retirement, many advisors will tell you that in this race against time you win when you hit a magic savings number. When we go to the videotape (or in our case an Excel spreadsheet), we realize that isn't the correct focus. Instead, we should be asking, "Do I have enough *income* to retire?"

What you hear vs. what you need

When working with a financial advisor (either large or small) who concentrates on helping you grow and then spend your savings, you will hear about positive steps to take, such as contributing the maximum to your 401(k), diversifying your investments, and seeking low fees. All good things to do.

Most advisors also talk about asset allocation, probabilities and market averages. They encourage saving but don't discuss the best ways to convert those savings to steady income. Instead, when advisors give guidance on spending down your savings, they usually mention investing more in fixed income investments, and possibly downsizing your budget to make your savings last longer. With this spend-down strategy, you are taking 100% of the risk, whether from market volatility or from longevity.

Finally, ask your advisor about strategies that incorporate the most obvious "income" vehicle that reduces your risk and your taxes.

Income Planning Starts with Income Allocation

The first word in retirement is income

When I think about retirement planning for Boomers, I have a laser focus on income, whether it is income allocation, income planning, income taxes or income annuities. This seems like common sense to me, since the universal retirement goals include:

- Maximize Social Security **income**
- Minimize taxes on **income**
- Allocate a portion of savings to lifetime **income**
- Reduce or eliminate **income** volatility
- Generate predictable **income** to cover essential expenses
- Generate secure **income** to cover late-in-retirement expenses

Three steps to income allocation

Income allocation has as its goals to both increase the amount of after-tax income (spendable) and to reduce income volatility (dependable).

Here are three steps to take to improve your retirement income:

Step 1 - Include income annuities as a new asset class. Sounds reasonable to include an investment that pays you a monthly income, is guaranteed by an insurance company rated "A" or better, starts at a date you select. and continues to you and your spouse for life. You can read more information here and here on the benefits of including income annuities in a retirement portfolio.

Step 2 - Treat your rollover IRA accounts differently than your personal (after-tax) savings. The tax treatment of each account is so different that it's almost negligent if your advisor recommends the same allocation for both. One simple example we'll analyze in Part III is the adoption of very different equity portfolios in the two types of accounts.

Income Planning Starts with Income Allocation

Step 3 - Manage withdrawals from your rollover IRA savings rather than simply taking the IRS-mandated required minimum distributions. By manage, I mean to adopt an investment strategy/withdrawal formula that reduces your risk and integrates with the income annuity cash flow. Remember, the IRS is just trying to collect some tax dollars and not to create a retirement plan for you.

Asset class designation for income annuities

- An asset class is a group of securities that exhibits similar characteristics, behaves similarly in the marketplace and is subject to the same laws and regulations. The three main asset classes are equities, or stocks; fixed income, or bonds; and cash equivalents, or money market instruments.
- Does an asset class, have to be traded or have liquidity? An asset's illiquidity does not speak to its return potential. It only means it may take more time to find a buyer to convert the asset into cash.
- So, what is the missing asset class? It's been hiding in plain sight – doing its job for the past 100 years. It's called an "income annuity." It's like a customized pension that you purchase with your own money. Also, according to Treasury rules, income annuities have a fair market value that must be reported to you in certain situations.

Crunch the numbers

With these three pieces of income allocation in place, advisors will need to build their own algorithm for figuring out how much and what type of income annuities should be included, what tactics to employ on the investment side, and how to determine the client's need for income, both early and late in retirement.

While the numerical analysis will be important, the most important benefit may be an asset that's not recorded on your balance sheet: Peace of mind.

Study Confirms: More Income with Less Volatility

Obviously, I believe that you could receive more retirement income with less volatility if you and your advisor moved from asset allocation to income allocation. It's one thing to suggest it and another thing to prove it. So we conducted a study comparing the results of asset allocation and income allocation strategies under various assumptions as to the retiree's risk profile and market outlook.

Not only did we observe more retirement income and less volatility, but we also saw generally higher economic returns. A copy of the study is available for free when you register on the Go2Income website.

We identified two new measures for our study:

- **Income Volatility:** The percentage of income that is dependent on the market value of the underlying investments (such as stocks or bonds). Volatility can be up or down, good or bad, but in all cases, it makes your planning uncertain.
- **Effective Rate of Return:** The constant rate of return on savings that produces the income and legacy benefits that emerge.

Having a higher economic return in addition to the features and soft benefits described below makes a strong case for the income allocation strategy.

Sample Case

For this eBook, we selected the following case from our study: Male, 70, who has $1 million in retirement savings, with 50% in a rollover IRA. His risk profile is conservative, with an asset allocation of 30% to equities, based on the "100 minus age" rule of thumb, and 70% to fixed income securities.

We compared the asset allocation strategy to an income allocation strategy with a high allocation to income annuities. Both strategies assume identical market returns.

Here are some highlights of the results of income allocation in this case:

- Before-tax income is increased by 42% over the investor's lifetime.
- Income volatility is reduced from 69% to 19%.

The investor can spend the extra income or reinvest it to leave a legacy as much as 29% higher.

Study Confirms:
More Income with Less Volatility

Sound too good to be true? Let me walk you through the numbers and the explanation for these advantages.

Review of Income Allocation Strategy

The twin goals of income allocation are to increase the amount of after-tax (spendable) income and to reduce income volatility (for more dependability). Here are the three steps that distinguish the income allocation strategy from virtually all other retirement planning strategies.

1. Include income annuities as a new asset class and consider them as part of the allocation to fixed income investments, along with bonds and CDs.
2. Treat rollover IRA accounts differently than personal (after-tax) savings accounts in managing the equity portion of your portfolio.
3. Manage withdrawals from rollover IRA savings rather than simply taking the IRS-mandated required minimum distributions.

The advantages come from holdings that generate the highest amount of dependable, spendable income. The greater allocation to dependable income continues for the retiree's life, with all withdrawals eliminated by age 85—what should be the retiree's worry-free age.

The study will go into considerable detail on methodology and assumptions.

What an income allocation plan does for an investor

The case study summarized in Table 1 quantifies the benefits for our investor. It shows an increase in first-year income of 21% (from $43,182 to $52,381 and a 32% decrease in income volatility.

Study Confirms: More Income with Less Volatility

Table 1 - Sources of Income in Year 1		Traditional Asset Allocation	Income Allocation
IRA	Withdrawals	$29,682	$19,536
	Annuity Payments	$0	$11,663
	Total IRA	**$29,682**	**$31,199**
Personal Savings	Dividends	$3,000	$7,031
	Interest	$10,500	$6,375
	Annuity Payments	$0	$7,776
	Total Personal Savings	$13,500	$21,182
	Total PreTax Income	**$43,182**	**$52,381**
	Taxes	$12,858	$12,629
	Total After Tax Income	**$30,324**	**$39,751**
	Income Volatility	**69%**	**37%**

Of course, everyone is different and any conclusion you make should be based on an illustration designed specifically for you.

The advantages derive from a focus on holdings that generate the highest amount of dependable, spendable income, as suggested in Table 2.

Study Confirms: More Income with Less Volatility

Table 2 Allocation of Retirement Portfolios			
		Traditional Asset Allocation	Income Allocation
IRA	Equities	$150,000	$112,500
	Fixed Income	$350,000	$112,500
	Income Annuities (A)	$0	$275,000
	Total IRA	$500,000	$500,000
Personal Savings	Equities	$150,000	$187,500
	Fixed Income	$350,000	$212,500
	Income Annuities (B)	$0	$100,000
	Total Personal Savings	$500,000	$500,000
	Total Retirement Savings	$1,000,000	$1,000,000

(A) Combination of QLAC and Immediate Annuity
(B) Immediate Annuity

Beyond the Numbers

While the study quantifies the dollar-and-cent advantages, the real upside, or "soft power," may be the qualitative benefits—which in turn may also create even more advantages not accounted for in our study.

What do I mean by soft power? By providing more income with less volatility, the investor achieves peace of mind knowing that income is less dependent on the market, continues for life, and is more certain. Besides less "angst," the investor is much more likely to stay the course.

One can imagine what investors might do during a major correction when 50% or more of their portfolio is dependent on market results. Typical retirement planning leaves the investor with plenty of uncertainty.

If you have a question about how income allocation might work you, post your request on Ask Jerry.

About Jerry Golden

Jerry Golden is a nationally recognized advocate for retirees (and for those planning their retirement) whose retirement can last two or three decades or more. He is responsible for many of the landmark innovations that have helped consumers achieve financial security during their entire lifetime. As an innovator, Jerry has often had to challenge the accepted wisdom of both product providers and distributors, and drive regulatory change where necessary.

His interest in annuities and their unique ability to produce guaranteed lifetime income for consumers (just like Social Security or a pension) began years ago with his first assignment out of college. As an actuarial trainee at The Equitable just graduated from the University of Michigan, Jerry's job was to review the pricing methodology for immediate annuities.

Jerry was impressed with their ability to address the basic question so many retirees have: *Will I have enough money to enjoy retirement and not outlive my savings?*

He saw this product as win-win for consumer and company, shifting the longevity and investment risk from the individual to the insurer. This risk-shifting plus a competitive marketplace made these income annuities an attractive deal for the consumer.

Jerry carried this viewpoint into his pioneering work on variable life insurance and variable annuities, where he innovated numerous times, building these product lines into billion-dollar businesses. In this work Jerry has always looked for tax-efficient designs, and encouraged market-based investing by expanding investment choices and combining them with various forms of downside protection.

With the intersection of investments and income annuities Jerry brought together:

- the first variable annuity with a living benefit guarantee (AXA Equitable Accumulator).
- the first rollover IRA account investing in income annuities (MassMutual Retirement Management Account).
- the first online integration of income annuities into retirement portfolios (Golden Retirement Savings2Income).

About Jerry Golden

Jerry is a sought-after speaker and industry panelist, and has appeared on Bloomberg Radio, Fox News, and CNNfn. His research has been featured in leading financial publications including Bloomberg Online, Huffington Post and Kiplinger's Retirement Report, along with numerous trade publications and daily newspapers.

His executive experience includes:

- President, Income Management Strategies Division of MassMutual
- Executive Vice President, AXA Equitable
- Founder and President, Golden American Life
- President, Monarch Resources, Inc.

Today Jerry is founder and CEO of Golden Retirement LLC, where he is delivering his unique expertise to consumers by helping them create retirement plans that provide income that cannot be outlived. His innovation continues with Go2Income, where you can explore all types of income annuity options, anonymously and free of charge. The result is a personal approach that allows consumers to create *dependable, spendable retirement income* that will last a lifetime.