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inside:

THE WORKPLACE

When Do You Plan to Retire?

by Ray Swartz

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Ray Swartz started his financial plan in 1988. He has been "voluntarily" unemployed since January 2001 and doesn't plan to work in 2002, either.

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[Editor's Note: Ray will be writing occasional columns on financial planning. I think many of our members are beginning to consider such things. RK]

Retirement means different things to different people. To some, retirement is playing golf every day. To others, it is traveling to faraway places. Some people don't have an interest in ever retiring. In fact, every person's retirement ideal is unique to them and their circumstances.

What is the same for all of us is the desire to have the money and time to do whatever it is we want to do when we stop working. For most people, this doesn't just "happen." It is something you have to plan for and arrange, usually over a period of years.

Many people view retirement planning as "saving as much as you can and putting it away until you need it." But this one-size-fits-all strategy may or may not work. It ignores these questions:

- How much do I need to retire?
- Where should the money I "put away" go?
- When can I stop working?
- Am I saving too much and sacrificing my current needs and wants?

While "saving as much as you can" is not a bad idea, it provides no real guidance about what to do today, nor is it based on any current need or desired outcome. A better approach is to put together a plan that takes your current situation and future needs into account and provides benchmarks for checking that your plan and results are on target. Without question, to have a nice retirement you have to plan to have a nice retirement!

A Desire to Retire

The first step in retirement planning is deciding what "retirement" means to you. Since retirement planning is about money, you should decide if you want to continue to work (part-time, project contracts, in a different field, etc.) as part of your retirement. That is, will you have to fund your retirement entirely from savings and investments or can you rely on some income?

You need to determine when you would like to retire. That is, in how many years do you plan to stop working? Often this will be determined by your company's pension arrangements or other commitments you might have. On the other hand, answering "as soon as possible" is perfectly acceptable, too.

Part of this process is trying to calculate how your retirement life will be different from your current one. Specifically, you need to estimate how your spending needs might change. Are you planning to go on cruises six months of the year? Do you want to move to Hawaii, where the cost of living is higher? What about increased health costs as you age?

As an example, suppose that you now spend your vacation time working around the house or driving to a friend's house in a nearby city. When you retire, you want to travel the world four months out of the year. In this case, your travel expenses will dramatically increase when you retire.

It may seem unrealistic to even guess what your expenses might be in future. You aren't looking for accuracy here. You only want to catch the obvious differences. There's a rule of thumb in the financial planning community that can provide guidance: absent unusual plans, the assumption is that retirement expenses will be 75% of what they were pre-retirement. Note that some of the uncertainty may be removed using insurance and other investment options.

Getting There from Here

Once you rough out your retirement plans, you can start to put numbers to how much retirement will "cost" you. The next question is can you afford it? Put another way, what do you have to do today so that you can retire when and how you want?

The answer depends on your current financial situation. Given what you have invested, how much you make (and are likely to make in the future) and how much you spend, what, if anything, do you have to do to reach your retirement goals?

Your investments consist of retirement accounts, insurance policies, and any other monies you might have. Unless you plan to sell your house, don't count the equity in your house. After all, you have to live somewhere. The benefit of paying off your house (if you have one) is that you have no rent expenses.

In addition to salary, calculating what you make should include any rental properties, interest, and capital gains. This information is easily found on your yearly 1040 tax form. In my experience, people generally know how much money they have coming in.

The most challenging number you need to come up with is your yearly expenses. This can be difficult as most of us aren't accustomed to thinking in terms of annualized costs. For example, how much do you spend on clothes each year? How about house maintenance? Also, don't forget the interest you pay on credit cards or your mortgage.

The best way to determine your yearly expenses is to look through your checkbook. I like to put things in categories so I know where the money is going. However, simply knowing how much you spend is good enough for a first cut.

To make my life easier, I run all my expenses and ATM withdrawals through the same checking account. This makes collecting expense data much easier. If your situation is more complicated, you may find that you have to paw through several accounts to gather all this information.

Things that won't show up in your checkbook include car depreciation, taxes withheld from your paycheck, and expenses paid in cash. Car depreciation represents the amount of money you will have to spend when you replace your car. If you pay cash or take out a loan, you want to be sure and account for this future outlay of cash somehow. In order to fully understand the income and outgo of your financial system, you need to add-in taxes you pay. You will probably be shocked at how much it is! Also, be sure to capture how much cash you go through. I add up all my ATM withdrawals as a proxy for the amount of cash I spend.

The first time you try to determine these numbers may be a real challenge. However, keeping track of it after that is generally a breeze, once you know where everything is. Your reaction to even thinking about doing this might be one of shock and horror. But I urge you to stick with it. The information is invaluable to securing your financial future.

Constructing a Plan

After assembling a retirement scenario and calculating how much you have, make, and spend, you can determine where you stand. You may be surprised to discover that what you have been doing is adequate to meet your retirement goal. If not, you can find out

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what you have to do to make your plans work. In some cases, the numbers may tell you that your dreams are a bit unrealistic and you need to scale them back or put them off a few years.

Even if you do nothing more than assemble this data, you will get a clear view of your current financial position. Knowing how much you spend in relation to how much you make is an important step toward achieving your life goals, whatever they are.

Creating a retirement plan involves combining your current resources with your income and expenses to create an *investment* plan that will deliver the amount of money you need to have when you want to retire. For most people, this will require the help of a professional financial planner and the will power to stick to the plan.

Also, retirement is not the only component of a financial plan. You also need to think about funding your children's education, making arrangements for your estate, and insuring or otherwise taking care of other problems that might arise in your special situation. A finance professional should know what is best for you after reviewing your specific particulars.

Aren't All Money People Slimy?

There are many kinds of financial planners: stockbrokers, insurance hawkers, annuity pushers, and assorted other creatures in the money jungle. Since they tend to get paid when you make investments they recommend, there is plenty of room for double-dealing and hidden self-interest.

Here are some basic guidelines to follow when choosing a financial advisor.

First, your finance person has to get paid. Find out how they get paid and make sure that you are comfortable with that. Ask questions about how the advisor gets paid. Don't even think about doing business with people who are vague about where their money comes from. Is what they recommend limited by what they make a fee on? What other charges might there be on your account?

Not all financial advisors are created equal. In theory, they all have passed the same tests given by the state where they are practicing. However, they all have their own biases and motivations. It is unlikely that choosing the first one you find (or who finds you) is the best approach. I suggest getting recommendations from people you trust, asking for referrals, and looking around. Avoid anyone who makes investments suggestions without first evaluating all the data discussed above. No one can advise you on what to do until they fully understand what you are trying to accomplish.

When you begin talking to people about finances, you will get a lot of unsolicited advice. People will brag about their financial wizardry, give you some hot stock tip, or provide other gems of financial hokum. Just nod your head and move on. Remember that you want to construct a future based on your unique needs. Any advice you get that doesn't take that into account should be ignored.

Lastly, not all financial advisors are greedy scumbags looking to get their hands into your pockets. Good financial planners are like good dentists: they may occasionally inflict pain, but in the end you will be better off for following their advice!

The most important point is this: it is up to you to create your own financial future; no one else will do it for you. Having and following a clear financial plan takes a lot of the uncertainty out of the future and gets you much closer to doing what you want when you want.