

# 10 MISTAKES PEOPLE MAKE IN RETIREMENT

by Bill Elson, CFP®

3705 Grand Avenue Des Moines, IA 50312

(515) 255-3306 or (800) 616-4392

[bill@sfsplanners.com](mailto:bill@sfsplanners.com)

KEYWORDS: RETIREMENT PLANNING, RETIREMENT INCOME, RETIREMENT CALCULATOR, RETIREMENT AGE, RETIRING,  
RETIREMENT PLAN

## RETIREMENT MISTAKE 1:

### NOT KNOWING HOW MUCH MONEY IS ENOUGH TO RETIRE ON.



People often sway to one extreme or the other when deciding whether they have enough money to retire on. Some people feel very confident retiring with a portfolio that *sounds* like a lot of money to them. They don't consider inflation, underestimate their retirement expenses, and rely on Social Security stability and consistent investment returns. These mistakes can eventually cause you to risk running out of money.

On the other hand, we see many people who have large retirement portfolios along with pension plans to supplement Social Security coupled with relatively low living expenses who appear to have a very high chance of financial success in retirement. Yet they are insecure about their wealth and feel like they need to keep working or they will run out of money.

The amount of money you need for retirement is a judgment call and there are many assumptions to make such as return on investments, living expenses, inflation rate, and the future of Social Security. It does not make sense to make the retirement decision, which is often the most important financial decision one makes in life, without a well-thought-out retirement plan and projections that show that retirement is feasible with assumptions and risks you are comfortable with.

## Retirement Mistake 2:

### DRAWING TOO MUCH MONEY FROM YOUR PORTFOLIO IN THE EARLY YEARS.

Many financial experts agree that it is okay to maintain a 3% to 4% annual withdrawal rate as a young retiree, meaning someone with a \$500,000 portfolio at age 62 could draw \$15,000 to \$20,000 per year with a reasonable chance that as expenses and withdrawals increase due to inflation, they will not run out of money.

Investment returns, inflation, and life expectancy all play important roles in establishing a withdrawal rate from your portfolio.



Also, discipline plays an important role. Taking additional lump sum withdrawals for purchases, home improvements, travel, family loans or other non-essential reasons is not a good practice if you have already established a sustainable withdrawal from your portfolio. It is important to consider the long-term impact on your retirement security when considering a significant withdrawal as the "extra" withdrawals can tip the scales so that your portfolio does not last as long as you do.

## **Retirement Mistake 3:**

### **UNDERESTIMATING YOUR RETIREMENT LIFE EXPECTANCY.**

We typically ask retiring clients how long they expect to live as well as gather data on the age and causes of family members' deaths or their track record of family longevity.

Many clients underestimate their life expectancy. For example a 65 year old couple might say they expect to live to 75 because they heard that is the average age of death of Americans. However, according to IRS Publication 590 (2010), at age 65, your life expectancy is 21 years. The Annuity 2000 Mortality Table suggests that the life expectancy for one member of a 65 year old couple is 92. Advances in medicine are further advancing life expectancies.

We see others who at 65 may say they will probably live to 95 because both of their parents are that age. But they usually don't think about the changes they will have in the next 30 years in expenses, health and other areas. Just take a look back 30 years and see how much different life was then compared to today. What did you spend 30 years ago relative to today? At a moderate inflation level, your expenses double every 20 years or so. Have we planned for that?

From a financial planning perspective the worst case scenario is that you live a long time and the best course of action is to develop a plan that addresses the financial risks of longevity.

## **Retirement Mistake 4:**

### **IGNORING HEALTH INSURANCE DECISIONS IN THE PLANNING PROCESS.**

People retiring prior to the Medicare age of 65 often pay tens of thousands of dollars for medical insurance. Many company-sponsored health insurance plans retirees' have reduced benefits and increased prices dramatically in recent years, and there is no guarantee the plan can't change for the worse or even terminate in some cases.

Medicare itself has significant financial problems and was recently projected to be insolvent in 2017 unless more tax is collected. In addition, in most cases Medicare does not cover long term health care which can be one of the most expensive health-related expenses a retiree faces. It is easy to put off making a decision about purchasing long term health care insurance but it's one that is important to address while you are relatively young, healthy, and able to qualify for the coverage.

Choosing a Medicare supplement has become very complicated with the addition of Medicare Advantage Plans and Part D drug coverage. Most people can benefit from help with this.

## **Retirement Mistake 5:**

### **NOT FULLY UNDERSTANDING SOCIAL SECURITY OPTIONS.**

Most people who retire before full retirement age (currently 66) focus solely on the decision of whether to take Social Security at retirement or wait until full retirement age with a larger benefit. This is an important decision but the numbers are relatively easy to crunch if you are able to make a few assumptions.

Over the years we have uncovered many nuances to the Social Security program. Examples include:

- Ability to start and stop Social Security benefits
- Effect of working while receiving Social Security benefits
- Widow and widower benefits starting at age 60
- Benefits from ex-spouses
- Non-working spousal benefits

It is important to understand all facets of this program that can affect you personally. To make this decision one must look at the break-even age and consider the possible future changes to Social Security.

## **Retirement Mistake 6:**

### **BEING TOO CONFIDENT IN YOUR INVESTING SKILLS OR LISTENING TO THE WRONG PEOPLE.**

Many people gain confidence by watching financial shows on television, reading newsletters or listening to talk radio. They learn something which may be good information, but then feel like they know all they need to know about money management. The truth is, the investment landscape is constantly changing and products are continually evolving. Someone who does this part-time or with snippets of information cannot do it as well as an experienced professional who works at it daily.



Many stories about investment success that are told by friends and associates are attributable to their being lucky and not skilled. In addition, most people don't like to talk about the investment mistakes they have made. They tend to leave those out of the conversation.

## **Retirement Mistake 7:**

### **BEING EMOTIONAL ABOUT INVESTMENT DECISIONS.**

One of the most common mistakes people make is “emotional investing”. Fear and greed are the main forces at work here. People tend to be fearful and want to sell at the worst times - when they have sustained a severe loss. Conversely, when investments are doing well, people allocate more money to them. Essentially they are buying high and selling low – the opposite of what one is supposed to do.



Dalbar, Inc, an independent market research company, found that in the 20-year period ending in 2008, the S&P 500 stock market index returned 8.35%. However the average investor who bought equity investments only earned 1.87%, which was less than the inflation rate. The primary cause of this is emotional investing. In 2000 when the market was peaking, it seemed like everyone was an expert on buying technology stocks and making huge sums of money which soon vanished when the market crashed. Then at the bottom of the crash in 2002, which was a good time to invest, people would not do so because they were afraid. Again, this is the opposite of the “buy low, sell high” method that brings investment success, and it is investor emotions that are primarily at fault.

## **Retirement Mistake 8:**

### **FAILURE TO FULLY EVALUATE PENSION OPTIONS.**

Many companies and government employers offer defined benefit pension plans that offer monthly income for life and sometimes an option to take a lump sum cash withdrawal to rollover into an IRA account.

Every plan is different. Some have excellent payouts if you take the monthly income instead of the lump sum. On other plans you may have a chance to generate more income by taking the lump sum. It usually depends on your age at retirement, salary, and years of service, so it is not always good to “do what everyone else does”. Some factors involved in the decision are:

- How long do I (and my spouse) expect to live?
- How much of a reduction do I have to take to give my spouse a good monthly benefit?
- Can I buy life insurance for my spouse cheaper than taking a reduced benefit?
- Does the plan offer inflation protection?
- How safe are my pension benefits?
- What is a reasonable income to expect if I take the lump sum?

Careful analysis can usually spell out the best option for your situation.

## Retirement Mistake 9:

### FAILURE TO DIVERSIFY YOUR RETIREMENT PORTFOLIO.

A general rule of thumb is not to place more than 10% of your portfolio in one investment and not more than 5% in an individual stock or bond. Following are some questions to ask on portfolio diversification:

- How big of a loss could I take without significantly affecting my retirement?
- Do I have too much in my company's stock?
- Am I over FDIC insurance limits on my bank amounts?
- Do I have most categories or styles of stocks and bonds represented in my portfolio?
- What is my investment plan to protect against inflation?
- Should I allocate some money for guaranteed retirement income in an immediate or deferred annuity?
- What types of risk do I need my investments to guard against?

\* Diversification does not guarantee a profit nor guarantee against a loss.

Change in Price	Current level	Bid (%)
+139.61	1,953.38	6.3
-0.11	3.55	3.0
+58.26	1,889.50	11.31
+321.89	7,850.29	1.31
+34.74	835.32	1.31
+70.59	1,210.48	14.55
-497.94	8,529.51	6.75
+216.12	2,930.74	6.94
+136.37	2,902.27	1.55
+29.10	856.56	16.27
-85.67	8,965.70	10.36
-17.12	7,039.25	3.44
-61.40	2,883.00	
+3.05	132.21	

## Retirement Mistake 10:

### NOT STARTING EARLY ENOUGH.

A rule of thumb is that one should save 10% of their income for retirement, about double what the average American saves. It is important to take advantage of time. People who start young take advantage of the power of compound interest. It's easy to start saving for retirement by having money deducted from your paycheck or bank account.

As a hypothetical illustration of the power of compound interest, take for example the case of Investor A and Investor B. Investor A begins saving \$2,000 per year at age 25 and continues to do so for 10 years and stops. At a 6% rate of return, the total investment of \$20,000 would grow to over \$150,000 at Investor A's age 65! Investor B, on the other hand, waits until age 35 to begin saving. He puts away \$2,000 per year for the next **30 years**. At his age 65, a 6% return on his \$60,000 total investment would leave him with just over \$158,000. Investor A saved less than one-third as much as Investor B, but because she was invested for a longer period of time, compounding interest yielded a similar retirement nest egg. This example is for illustration purposes only as actual results will vary.

One of the most common things people say when they meet with us for retirement planning is “I wish I had done this years ago”. Don’t procrastinate. Start retirement planning now.

#### About the author

Bill Elson, CFP® is a Certified Financial Planner™ practitioner that operates his financial services business in Des Moines, Iowa. Bill offers Investment Advisory Services are offered through Legacy Financial Group, LLC, doing business as Spectrum Advisory Services, a registered investment adviser. Securities are offered through Broker Dealer Financial Services Corp, Member FINRA & SIPC. Broker Dealer Financial Services and Spectrum Advisory Services are not affiliated.

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