Will You Be Able to Retire?

Yes, But Only If You've Effectively Planned Out A Strategy

by **Doug Wheat, CFP**, published in the July issue of Healthcare News

Make no mistake, your financial future is up to you. Not your employer. Not the government.

The average life expectancy of someone who is 65 today is 87 years of age. If you retire this year, you can expect to spend 22 years in retirement. Also, if you are married at age 65, there is an 18% chance that either you or your spouse will live to be 95, according to the Society of Actuaries retirement table. When you retire, you need to be financially prepared to meet your evolving needs for many more years.

Individuals who earn $250,000 or more a year often fail to save enough to retire in the lifestyle to which they have grown accustomed. That may sound ridiculous, but doctors, lawyers, and others who earn big salaries often fail to grasp their retirement-savings shortfall.

What causes high-income earners to miscalculate such a critical issue? Often the mistake is assuming that saving $20,000 or even $30,000 a year ensures a comfortable retirement. Other times, people just fall into the trap of spending everything they earn.

Meet Ray and Nicole

Let's look at the case of Ray, a 40-year-old dermatologist, and his wife, Nicole, who have a 6-year old daughter and a 4-year old son. Ray earns $240,000 per year, while Nicole does volunteer work and takes care of the kids. They pay about $62,000 a year in federal and state taxes, and another $8,000 goes to pay FICA and Medicare taxes. An additional $10,000 is withheld for medical insurance. That leaves them with approximately $160,000 for expenses, debt payments, college funding, and retirement savings. It should be plenty, right?

For Ray and Nicole, mortgage payments total $30,000 annually, and medical-school debt payments are another $14,000. They set aside $500 per month in a college fund for each of their two kids, which is an additional $12,000 each year.

Ray, now a partner in a small practice, socks away $30,000 a year in a profit-sharing plan at work. He and Nicole already have $140,000 in retirement savings in IRA accounts.

This leaves them with $74,000 a year to live on, which gets spent on food, clothing, utilities, two cars, vacations, house maintenance, their kids' activities, charity, and gifts. They spend everything they earn. Last year they even had to dip into savings to pay for repairs to their roof.

Both Ray and Nicole think they are doing everything they can to save for retirement and their children's college education while not living a very extravagant life. They are optimistic they will be able to continue their current lifestyle in retirement. But the numbers indicate it is not a slam dunk.

Crunching the Numbers

Let's assume that Ray makes $30,000 annual contributions to his profit-sharing plan for the next 25 years. Also assume his profit-sharing plan earns 7% annualized return in a balanced portfolio over that same time period. At age 65, when Ray and Nicole plan to retire, their next egg will have grown to about $2.9 million. That sounds like a lot of money, right?

Actually, it may not be enough based on their current standard of living and some additional travel they would like to do. The projections indicate they would run out of money by the time Ray is 88 and Nicole is 86. That leaves them little breathing room if they live into their 90s or if the returns on their portfolio turn out to be less than 7%.

For a point of reference, the value of $2.9 million in 25 years is equivalent to approximately $1.4 million in today's dollars, assuming a modest 3% inflation rate. So Ray and Nicole are not as rich as it seems, and, making realistic assumptions, their retirement can turn ugly even with a $2.9 million nest egg. This also assumes they receive Social Security adjusted upward by 2% a year.

To top it off, Ray and Nicole will probably not have enough money saved for college if their kids select some of the most expensive private schools.

Ray and Nicole obviously need not despair. Their current and future lifestyles exceed the vast majority of people. Yet, by not planning properly today, they increase the likelihood that they will have to either scale back their retirement or run out of money.

Even for high-earning individuals, saving for retirement requires discipline and proper planning.

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