An Income Strategy for a Couple with $200K

By Kerry Pechter *Thu, Apr 12, 2018*

Joe Tomlinson, an advisor who often recommends immediate annuities in income plans, takes a different tack in his plan for a hypothetical couple, both age 65.

At Wegman's supermarkets in the northeast, you often see people in their late 60s working part-time at cash registers, or tempting shoppers with trays of finger-food, or even refilling the shelves as what (in pre-Universal Product Code, pre-gender-neutral days) were called "stockboys."

When asked, some of these older workers say they work to "stay busy," or to "get out of the house." Some are taking advantage of Wegman's health care benefits. But many are probably doing it to delay spending their savings, or to bolster their savings, or to delay claiming Social Security benefits.

If so, they're following state-of-the-art advice. Many academics and advisors agree that "constrained" retirees (those with marginal savings) can best avoid running out of money later in life by delaying retirement and benefits Social Security until age 70. It's not easy or popular, but it's possible.

Take a recent **article** by Joe Tomlinson in *Advisor Perspectives*, for instance. An actuary and CFP, Tomlinson writes frequently about retirement income planning. In many of his articles, he recommends the purchase of single-premium immediate annuities, or SPIAs, for financially "constrained" retirees.

In this article, he doesn't. Instead, he recommends working longer and maximizing Social Security benefits as the best retirement income plan for a 65-year-old couple with a combined pre-retirement income of $75,000 and a retirement income need of $60,000 a year.

The hypothetical couple lives in paid-off home worth $200,000, qualifies for combined $28,000 a year in Social Security benefits at age 65, and has saved $200,000 (50% stocks, 50% bonds) in qualified (pre-tax) accounts. That's more savings than the median babyboomer has ($147,000, per a 2016 Transamerica survey) but much less than the couple needs.

But Tomlinson finds a solution, after considering a number of tactics. The couple can work to age 67 or to age 70, which raises their Social Security benefits, enhances their savings and reduces the number of years of retirement that will require funding. They can try using a reverse mortgage or opening a reverse mortgage line-of-credit.

Since their Social Security income will make up such a big fraction of their resources, they can afford to hold 100% stocks instead of 50%. He also tests the possibility of using savings to buy a SPIA for immediate income or a QLAC (qualified longevity annuity contract) providing lifetime income at age 85.

Tomlinson eventually recommends a strategy that require the use of home equity, working longer, delaying Social Security, shifting money to stocks and—crucially—using the required minimum distribution (RMD) method of decumulating the $200,000 in qualified money (where withdrawals starts at 3.65% per year at age 70 and gradually reach as much as 8.77% per year at age 90).

This strategy raises the couple’s income to almost $57,000 a year, or very close to their goal of $60,000. Just as importantly, it entails a portfolio failure rate (risk of having only Social Security to live on) of only 10%, Tomlinson figures. Working longer is an essential element to this strategy, because it saves the couple from spending more than half of their $200,000 in savings between the ages of 65 and 70. Equally important is a reverse mortgage tenure (a lifetime payment based on the equity in the house). It’s not so crucial that the couple move all their savings into stock.

“Delaying Social Security doesn’t increase consumption for this example, but it significantly reduces downside risk. The use of a reverse mortgage provides a significant benefit by accessing a new source of funds,” Tomlinson writes. The tenure form of a reverse mortgage provides a level payout for life. This strategy would leave the couple with enough liquidity to maintain the house, as required by the reverse mortgage contract.

“The biggest improvements in retirement prospects come from working longer. For those who don’t save enough, it is a big plus to have stable employment in a good job, and to keep building job skills while maintaining good health. More human capital makes up for less financial capital.”

As mentioned above, Tomlinson tested the use of a SPIA at age 70 with $82,000 (the amount left over after retiring at age 65 and spending $118,000 before age 70). He also tested the purchase of a QLAC (with income starting at age 85) with $20,000 of the $82,000. Neither of these strategies produced the most income, according to his calculations.

There are potentially hard-to-swallow trade-offs implicit in this strategy for the millions of American couples who are likely to find themselves in similar circumstances at age 65. To the extent a couple taps home equity for consumption, it won’t be available for health care expenses or bequests.

There’s also no overestimating the difficulty that some (though not all) people may have with the prospect of working until 70. People in marginal or poor health, people with physically demanding jobs, and people without accommodating employers may face barriers beyond their control. But, as Wegman’s older workers have learned and demonstrated, opportunities exist for those who look for them.