Edelman Financial Engines®

5 STRATEGIES TO HELP OPTIMIZE RETIREMENT INCOME

You spent your lifetime working hard, diligently saving and investing money to secure your financial future. But when it's time for retirement, how do you take income in a way that preserves your wealth as long as you need it to? The right strategy can help you manage taxes and maintain the standard of living you've been planning for.

In this guide, we'll first break down the potential risks to, and sources of, your retirement income. Then, we'll share five strategies to help you optimize your retirement income plan.

Most Americans worry about outliving their retirement savings. In fact, 33% of respondents in a recent survey by GOBankingRates said they're most concerned about running out of money in retirement.[1] No one wants to be in this situation, but it can happen if you don't have a plan.

Although setting retirement goals can be a time-consuming step, developing a strategy to fund your retirement is even more challenging due to the number of variables involved. Fortunately, there are planning and retirement income strategies that can help you feel more confident.

As you review the strategies later in this piece, keep in mind that everyone has unique needs and goals, and you may find it helpful to talk with a financial planner about your specific situation.

THE RISKS TO YOUR RETIREMENT

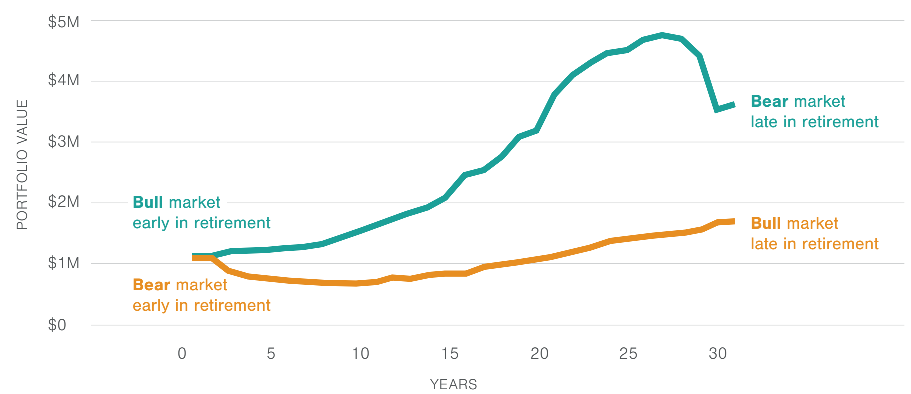
Outliving your retirement savings is always a possibility due to the nature of financial markets, the economy and health care costs. While these external factors are beyond anyone's control, what you can control is building a strategy that helps account for these risks.

High inflation – Some inflation is normal, and a solid retirement plan takes that into account. However, significant spikes can occur. For example, the Consumer Price Index rose more in 2022 than at any time in the previous 40 years.[2] If costs rise more than you expected when you built your plan, you may have to adjust your strategy.

Market volatility – Investors know there are always ups and downs in the market, but it's never good to see a lot of volatility or a large down market when you're in or approaching retirement. Volatility may make you reconsider whether you saved enough and makes it difficult to plan out your income strategy due to sequence of returns risk. That's the risk of running out of money if your portfolio is not able to sustain withdrawals after experiencing down years early in retirement.

Let's look at two hypothetical scenarios, both starting with $1 million with a 6.7% annualized return. In the first case, the retiree stops working during a bull market and experiences a bear market later in retirement. Their portfolio is able to continue growing during retirement even after accounting for regular annual withdrawals of $40,000. Then, by the time the bear market hits, their portfolio balance is large enough to weather it. In the second scenario, their portfolio goes through a bear market within the first five years of retirement, while they make $40,000 annual withdrawals. This causes their account to remain below the initial balance for nearly 20 years, which can certainly make a person feel less financially secure.

Sequence of returns risk in retirement



SOURCE: Edelman Financial Engines. This is a hypothetical illustration used to demonstrate the impacts of bull and bear markets on retirement assets either in the early years or later years of retirement, respectively, as withdrawals are taking place. Each scenario assumes a starting value of $1 million, annual withdrawals of $40,000, the same set of annual returns over a 30-year period, only in inverse order or "sequence." The orange line represents a sequence of returns that includes a bear market in its early years. The green line represents a sequence of returns that includes a bull market in its early years. Hypothetical performance of each line assumes a 6.7% average annual return over the full period. The chart is for illustrative purposes only and is not intended to predict investment results. They do not include consideration of the investment fees or expenses, time value of money, inflation, fluctuations in principal or taxes.

LIFE EXPECTANCY

17 YEARS

Additional life expectancy of a 65-year-old man

20 YEARS

Additional life expectancy of a 65-year-old woman

That's why market volatility is so dangerous. Your retirement income plan must be designed to help withstand multiple years of down markets early in retirement.

Health care – One of the biggest expenses during retirement is health care. The lifetime health care costs for a 55-year-old couple is projected to be over $1 million.[3] Even though your costs may be more or less, your plan needs to have a cushion and the flexibility to adjust as your situation changes.

Longevity – Depending on when you retire and how healthy you are, you could spend decades in retirement. A 65-year-old man has a life expectancy of an additional 17 years; it's an additional 20 years for a 65-year-old woman.[4] And all along the way, your plan needs to keep generating retirement income. Plan for it now to help avoid outliving your assets.

Taxes – Don't assume your taxes will go down in retirement. Just because you expect to have a lower income, that doesn't mean your tax rates will be lower.

Many retirement accounts provide tax advantages, but that doesn't mean they are tax-free. Distributions from 401(k) and 403(b) plans and traditional IRAs are taxed as ordinary income even though any growth is from investments. Up to 85% of your Social Security benefits are taxable if you earn more than $25,000 and file as single, or more than $32,000 if married filing jointly. Not being tax-efficient in your withdrawal strategy can cost you years' worth of retirement income.

WHERE WILL YOUR RETIREMENT INCOME COME FROM?

Your retirement income is likely to come from a variety of sources. Some are fixed sources that can provide a predictable amount of funds each year. Social Security is the most common example, and the benefit is based on your work history or that of your spouse. Employer pensions and annuities are two other income sources that can fund your retirement through regular, predictable payments.

Variable sources of retirement income include defined contribution retirement accounts, such as a 401(k) or 403(b), and brokerage and savings accounts. The income from these variable sources is not fixed. This helps add flexibility for your withdrawal strategy so it can be optimized for your situation but there is no guarantee how much you can withdraw at a time.

Finally, your retirement income may come from variable sources other than the savings you set aside. Many retirees choose to work part-time to keep busy and to provide extra income. You may also have income from rental properties or other noninvestment sources.

It's important to take the tax and distribution rules for all these sources into account as you establish your retirement income plan. Some sources may be better to tap into right away, while you should avoid taking withdrawals from others for as long as possible. As with most financial decisions, what you do should be based on your specific situation and an Edelman Financial Engines wealth planner is a good resource for help on these decisions.

The following five strategies can help you feel more confident that your plan will generate sufficient income throughout your entire retirement.

5 STRATEGIES FOR RETIREMENT INCOME

1. SET UP YOUR RETIREMENT ACCOUNTS WITH LONG-TERM GOALS IN MIND

It can be said that the stock market is the greatest wealth creator of all time, but it's a volatile and risky place. As mentioned earlier, this can make withdrawing from your retirement accounts more challenging due to sequence of returns risk.

You can help address this risk by focusing on long-term outcomes and maintaining a diversified portfolio that is rebalanced strategically.

> *The stock market has the potential to help you meet your goals, but only if you stay invested even during downturns*

Focus on the long term regardless of volatility. The stock market has the potential to help you meet your goals, but only if you stay invested even during downturns – trying to time the market is not worth the risk. Talking with an Edelman Financial Engines wealth planner when markets fluctuate can help you feel more confident in your plan and help you resist making changes based on emotion.

Diversify – Even in retirement, your portfolio needs the opportunity to continue to grow. It should align with your risk tolerance and be designed to support your retirement goals, which is why you need to maintain a diversified portfolio. Some of your portfolio assets may be negatively correlated, which means that when one changes, the other can move in the opposite direction. So when market volatility hits, your portfolio may go down, but a diversified approach can help soften the shock.

Your portfolio should also be constructed with tax-smart strategies in mind. Income from bonds and bond funds is taxed as ordinary income and may be best held in a tax-deferred account, such as an IRA. Stocks get more favorable tax treatment; most dividends from stocks and stock funds, as well as long-term capital gains, are taxed at only a 15% or 20% tax rate, which is something to consider for taxable accounts. However, you should have a properly diversified portfolio whichever type of account you have.

Strategically rebalance – The value of diversification is clear, but as some investments change in value over time, that original allocation between types of investments can be lost. Over time, your portfolio could possibly take on more risk than you'd prefer – or not enough. Rebalancing as needed can bring it back to the allocation level set out in your financial plan.

An Edelman Financial Engines wealth planner can guide you through the process of identifying your risk tolerance, income needs and spending flexibility to inform the construction of a balanced portfolio. The portfolio will then be rebalanced as needed during your retirement to help ensure it remains aligned with your needs and preferences. Your wealth planner will continue to partner with you, regularly discussing how your needs and circumstances may change and help you adjust your plan accordingly.

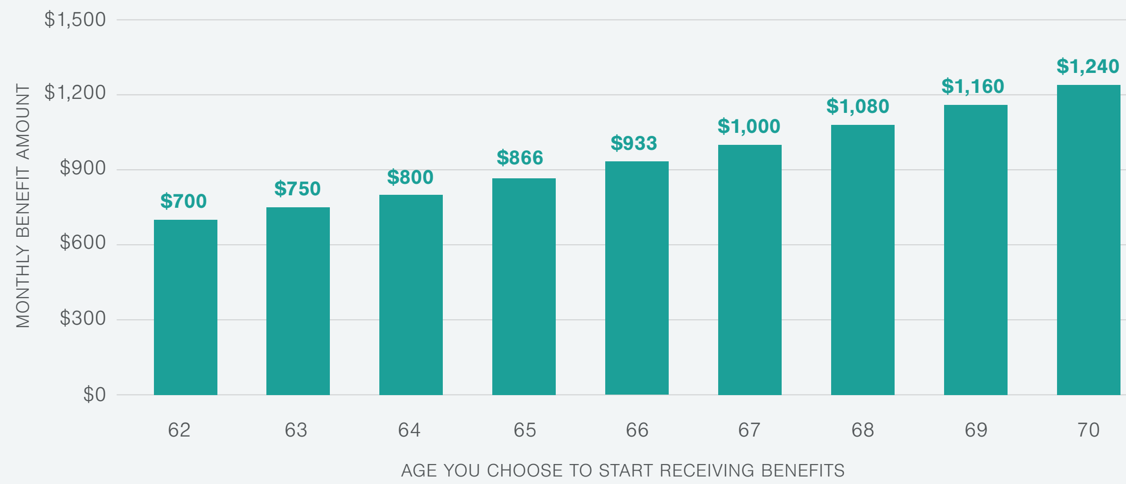
2. OPTIMIZE SOCIAL SECURITY

Social Security will likely be your only stream of retirement income with a cost-of-living adjustment (COLA). It's adjusted as inflation raises the costs of goods and services. But your plan for taking Social Security may not be as automatic as you think.

It's critical to develop a claiming strategy based on your specific situation. If you're single, your main consideration is deciding when to start taking Social Security.

Monthly benefit amounts differ based on the age you start receiving benefits

This example assumes a benefit of $1,000 at a full retirement age of 67



To get your full benefit, you need to retire at your full retirement age. It's 66 if you were born from 1943 to 1954, then increases gradually from 1955 to 1960 until it reaches 67. If you were born in 1960 or later, your full retirement age is 67. Even if you decide to retire early, it's usually best not to take Social Security earlier than your full retirement age.

For every year you wait to take Social Security beyond full retirement age, up to age 70, your benefit increases by 8%.[5]

Even better, future COLAs will be based on that bigger benefit.

Your decision becomes much more complicated if you're married. There are almost 9,000 possible claiming combinations, depending on the respective birth years. Married couples need to plan together to determine their strategy, just like they did for retirement.

For example, it may be advantageous for you and your spouse to claim benefits independently and at different times during your retirement. If one spouse has a benefit that is smaller than half of the other's benefit, he or she might be able to claim half of the larger retirement benefit, but there are rules that need to be followed. Or the spouse could file for their own benefits and then switch to a spousal benefit later.

If one spouse passes away, there is a survivor benefit for Social Security that introduces an entirely different set of rules and considerations that need to be addressed. Divorced spouses may also be able to claim benefits – either spousal or survivor benefits – on their previous spouse's work history if the marriage lasted for at least 10 years. Remarriage and your own retirement benefit may affect your options.

In all cases, it is best to check with the Social Security Administration on the benefits available to you. There are many rules and requirements that you'll need to follow, and an Edelman Financial Engines wealth planner can help you with the considerations as well as navigating the execution.

3. FOLLOW A WITHDRAWAL STRATEGY

Your withdrawal strategy should be part of your overall retirement plan. The strategy should consider your goals in retirement, your risk profile, your amount of savings, the types of accounts that hold those funds and your individual tax situation.

There are several different approaches to consider for a withdrawal strategy. The 4% rule is probably the most well known, which proposes that you withdraw 4% of your retirement savings each year. Some retirees may choose to withdraw a higher or lower percentage depending on their initial balance and the expected growth of their retirement portfolio.

A fixed-dollar approach is similar, but you take out the same amount of money each year for a set number of years instead of a percentage of assets. For example, if you had $1,000,000 saved for retirement, you may decide to withdraw $40,000 a year for the first five years and then reassess based on your needs and available assets.

Neither of these strategies is customized to your changing needs and they do not consider the potential tax advantages of withdrawing from certain retirement accounts in a specific order.

At Edelman Financial Engines, we often recommend using a withdrawal strategy that is based on your specific situation, including Required Minimum Distribution amounts, your tax brackets, other income sources and expenses. You may be able to prolong your savings by withdrawing money in the most tax-efficient order.

With a systematic withdrawal strategy, your investments are still diversified and include stocks, as opposed to loading up on bonds and taking only interest and dividends. Bonds are more volatile than consumers realize and don't always allow retirees to continue to grow their portfolios to support decades in retirement.

The systematic withdrawal strategy also defines how much can be taken out and when the withdrawals happen, such as monthly, quarterly or annually. The strategy essentially provides you with income during retirement while aiming to help minimize your taxes.

Another customizable approach that may work well is a bucket strategy. With this strategy, you withdraw assets from three separate accounts holding your assets.

The first account, or bucket, is for short-term needs and holds three-to-five years of living expenses in cash equivalents. The second bucket is for midterm needs and usually holds fixed income securities like bonds. The third bucket invests your remaining retirement savings in equities for long-term needs. As you use the cash from the first bucket, you replenish it from the second and third buckets.

No matter which withdrawal strategy you choose, it's important to stay flexible and work with your wealth planner to adjust your approach over time as your investment performance and life circumstances change. Family circumstances, personal health and even income needs can and do change, and usually when you least expect them. The more flexible you are, the more likely it is that you can maintain a lifelong stream of retirement income.

4. BE TAX SMART WITH YOUR RMDS

Required minimum distributions (RMDs) are an inherent part of retirement plans like 401(k)s and IRAs. These distributions may make up a good portion of your retirement income but there is not a lot of flexibility in how you take them.

RMDs exist to ensure you end up paying taxes on the money you saved. The passage of SECURE 2.0 at the end of 2022 raised the age when you have to start taking RMDs from 72 to 73 years old beginning in 2023. And that age will change from 73 to 75 years old beginning in 2033. Failing to take them can result in a tax penalty of 25% of the amount that should have been withdrawn and you still have to pay the regular tax too.

All defined-contribution retirement plan withdrawals after you retire are taxed as ordinary income, like a salary. That can affect the taxes you pay in ways you didn't expect. If you decided to work in retirement, your RMDs could push you into a higher tax bracket. Your Social Security benefits might be taxed at that higher rate too.

Of course, there are strategies you can implement to reduce the potential tax bite, such as making withdrawals from tax-deferred accounts before you turn 72, using Roth conversions, or making a qualified charitable donation directly from your IRA. Determining the best approach for you can be complex but when you develop a retirement income plan with an Edelman Financial Engines wealth planner, you can discuss making your RMDs as tax-efficient as possible.

5. A DECISION FOR PENSIONERS

If you have access to an employer-sponsored pension, count yourself lucky. What makes a pension great for retirees is that it is a defined-benefit plan entirely paid for by the employer and the benefit you receive in retirement is predefined.

Every pension plan is set up differently but, in general, the benefit is calculated based on a combination of salary and length of employment. The funds are then distributed to you and your spouse during retirement.

You can take your pension as a large lump sum or as an annuity that spreads out your benefit as equal payments over your lifetimes. That's an important decision to make that can impact your retirement income. As with most complex financial decisions, there are benefits to each approach and it is often helpful to discuss the choice with a financial professional.

Planning to secure your retirement income and feeling confident that you won't outlive your money is an important part of any financial plan.

> *At Edelman Financial Engines, we know that your financial life is complex, and a decision made in one area affects every other area.*

Our approach helps you balance all your financial goals while helping ensure you can establish an appropriate withdrawal strategy for retirement.

RETIREMENT PLANNING IS JUST ONE PART OF AN OVERALL WEALTH PLAN

Working with an Edelman Financial Engines wealth planner who understands your goals and unique circumstances is key to helping you grow, maintain, and protect your wealth both before and during retirement with a comprehensive financial plan.

Our aim is to help you achieve your financial goals, whatever they may be, as well as long-term financial security. Things like home purchases, children's higher education and estate planning are all taken into account as we help you develop your retirement withdrawal strategy.

Our integrated approach provides services for every aspect of your financial life:

- Financial planning
- Retirement planning
- Investment management
- Tax planning
- Insurance guidance
- Estate and legacy planning
- Small-business solutions

We offer investment advice with other financial services for the sophisticated needs of our clients. In addition, as a fiduciary investment advisor, our advice and management are provided only in the best interest of our clients. Fees are asset-based and transparent, meaning you'll know exactly where you stand, and can be confident you're getting objective advice.*

The portfolio management approach Edelman Financial Engines uses has been awarded 12 patents. Each month, we model more than 38,000 securities and build portfolios diversified across 16 asset classes. This allows us to analyze thousands of possible securities combinations to build customized investment strategies, taking into consideration time horizon, goals, preferences for risk and available investment funds.

* To find out more about Edelman Financial Engines' fees please visit www.EdelmanFinancialEngines.com/efe-form-crs/

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The *Barron's* 2023 Top 100 RIA Firms list, an eight-year annual ranking of independent advisory firms, is qualitative and quantitative, including assets managed by the firms, technology spending, staff diversity, succession planning and other metrics. Firms elect to participate but do not pay to be included in the ranking. Investor experience and returns are not considered. The 2018 ranking refers to Edelman Financial Services, LLC, which combined its advisory business in its entirety with Financial Engines Advisors L.L.C. (FEA) in November 2018. For the same survey, FEA received a precombination ranking of 12th.

LET'S TALK

We're proud to be one of America's largest independent Registered Investment Advisors, with many of our wealth planners holding the CERTIFIED FINANCIAL PLANNER™ certification or other independent professional designation.

Retiring is a significant transition in life and it's great that you want to learn more about how you can progress into it with confidence and a withdrawal strategy that delivers retirement income. With the support and professional knowledge from an Edelman Financial Engines wealth planner, you can maintain the same momentum in retirement that you currently have in your financial life.

Call **(855) 978-2336** today for help integrating these retirement strategies into your overall wealth management plan.

[1] Duley, M. (2023, May 19). *1/3 of Americans Are Worried They'll Run Out of Money in Retirement - Here Are 7 Tips to Make Sure That Doesn't Happen.* GOBankingRates.com. Retrieved April 17, 2024, from https://www.gobankingrates.com/retirement/planning/tips-make-sure-dont-run-out-money-retirement/

[2] U.S. Bureau of Labor Statistics (November 9, 2023). *Consumer Price Index for All Urban Consumers: All Items in U.S. City Average [CPIAUCSL]*. FRED, Federal Reserve Bank of St. Louis. Retrieved November 9, 2023, from https://fred.stlouisfed.org/graph/?g=8dGq Data through September 30, 2023.

[3] Assumes two years of health cost inflation at 1.5 times CPI of 7.9%. Source: HealthView Services, *2022 Retirement Healthcare Costs Data Report Brief,* Retrieved April 17, 2024 from https://hvsfinancial.com/wp-content/uploads/2022/03/HVS-Data-Report-Brief-0312222.pdf

[4] Social Security Administration. (n.d.). *Actuarial Life Table*. Retrieved April 17, 2024, from https://www.ssa.gov/oact/STATS/table4c6.html

[5] Social Security Administration. (2023, January). *When to Start Receiving Retirement Benefits.* Retrieved April 17, 2024, from https://www.ssa.gov/pubs/EN-05-10147.pdf

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Neither Edelman Financial Engines nor its affiliates offer tax or legal advice. Interested parties are strongly encouraged to seek advice from qualified tax and/or legal experts regarding the best options for your particular circumstances. Tax strategies is just one aspect of your overall financial plan.

Systematic Withdrawal Plans offer no guarantees. Withdrawing too much from your portfolio could cause your portfolio's value to decline. Your portfolio's value will fluctuate with market conditions. All investments have inherent risks.

Investing strategies, such as asset allocation, diversification or rebalancing, do not ensure or guarantee better performance and cannot eliminate the risk of investment losses. All investments have inherent risks, including loss of principal. There are no guarantees that a portfolio employing these or any other strategy will outperform a portfolio that does not engage in such strategies.

An index is a portfolio of specific securities (such as the S&P 500, Dow Jones Industrial Average and Nasdaq composite), the of which is often used as a benchmark in judging the relative performance of certain asset classes. Indexes are unmanaged portfolios and investors cannot invest directly in an index. Past performance does not guarantee future results.