

# Determining Cash Flow Need in Retirement



THE RETIREMENT GROUP<sup>LLC</sup>  
PARTNERS IN RETIREMENT



# **TABLE OF CONTENTS**

**01**

**Introduction**

**03**

**Data-Gathering**

**04**

**Cash Inflows**

**06**

**Cash Outflows**

**08**

**Impact of Taxes**

**09**

**Conclusion**

**10**

**Sources/Disclaimer**








# Introduction

When preparing for retirement it is important to understand cash flow to calculate income and liquidity needs to determine proper asset allocation and need to continue to work. Without understanding what the expenses will be relative to income, it makes it hard to properly determine just how aggressive someone needs to be with their investments and savings. Not everyone's situation is the same and therefore general asset allocation rules can't be applied in every situation.

In general, cash flow analysis compares income from all sources to expected expenses and liabilities to determine what liquidity needs will be (how much will need to be withdrawn from asset accounts). In addition to listing what your sources of income will be, it is important to consider the timing of these income sources (i.e. income from pensions, taking Social Security at 62 vs. 66, part-time employment).

It is important to do the same for expenses. For example, will you be going on vacations? Will you be purchasing a new house or car? What are the expected medical costs going to be? After listing all of the expenses, the timing of when this will be occurred is just as important as the type and amount.





Trying to pinpoint what your exact incomes and expenses is not an easy task, and it is impossible to predict what surprises will be incurred along the way. In this way financial planning is an art more than a science. For instance, maybe there is an unexpected repair needed for the home. You may have an unexpected medical expense or may not get that part-time job that was initially planned on. That is why it is important to update assumptions and recalibrate the financial plan at least annually as more information becomes available. It may become apparent that downsizing the house is needed later in retirement to meet a greater expense down the road.

The tax implications of timing your income or withdrawals makes it even more important to not only determine your income sources, but the planned timing of the income flows. Running different scenarios to simulate different outcomes in retirement can help in the simulation of what actual retirement could look like.

To plan for multiple scenarios, a financial planner can run simulations by going through the following process:



# Data- Gathering

To make an accurate plan, the financial planner will need as detailed information as possible. This information includes assumptions and facts provided directly by the client, and also information and assumptions provided by the financial planner based on their knowledge of economic and common retirement factors (inflation and life expectancy).







## Cash Inflows

As mentioned earlier, it is important to list all sources of income and determine the timing of those income flows. For instance, should you start Social Security at age 62 or delay to 66? If you have a work-sponsored pension plan, the main decision is how it should be received (lump sum or annuity? Single life or joint & survivor? Term certain or life expectancy?). Clients life expectancy and tax situation will have a major impact on these decisions. If a client wants to start a business or work part-time in the retirement, those inflows should be included too.

As an example, say you retire at 65, but want to delay social security to age 70 to maximize annual amount. To have income between ages 65 and 70 you purchase an immediate annuity with a 5-year payout period using non-retirement money. The inflow received will be parts principal and interested with only the interest portion considered taxable. Now at age 70 1/2 you are required to start taking annual required minimum distributions (RMDs) from your retirement accounts (IRAs, 401(k)s, etc.), and these withdrawals are taxed as income. If you are also working part-time during the period you are taking RMDs, this could increase your tax liability by pushing you into a higher tax bracket [3].



Polling data from Gallup in 2018 gives insight to sources of actual reported income from retirees' households [1,4]:

#### U.S. Retirees' Current Income Sources

How much do you rely on each of the following sources of income today -- Is it a major source of income, a minor source of income or not a source at all?

	Major source	Minor source	Total source	Not a source
	%	%	%	%
Social Security	57	33	90	10
A work-sponsored pension plan	35	22	57	42
A 401(k), IRA, Keogh or other retirement savings account	27	34	61	38
The equity you have built up in your home	19	29	48	52
Other savings such as a regular savings account or CDs	17	42	59	40
Individual stock or stock mutual fund investments	15	30	45	54
Annuities or insurance plans	9	20	29	71
Money from an inheritance	7	15	22	78
Part-time work	3	15	18	82
Rent and royalties	3	15	18	81

GALLUP, APRIL 2-11, 2018

It is important to understand the different income types that might be available and the tax implication associated with each.



## Cash Outflows

While expenses in retirement can vary, generally a person's current spending habits can be indicative of how they will continue to spend in retirement. While some people are very detailed about tracking their expenses, others might have a more general than specific idea. By tracking your expenses over time, it can help paint a more accurate picture for the person constructing the financial plan.

After determining the list of current expenses, unnecessary expenses can be eliminated from the plan or lowered to increased lifetime of assets. Other expected expenses such as paying for a family member's education or replacing a car should be considered to see how it affects the projection. Expenses should be categorized into core needs, wants, and wishes; that help determine which expenses should be cut out first, if needed, to ensure the success of the plan.

Health care costs are also a very important consideration especially as someone progresses through retirement or has a history of health issues in their family. These types of costs are generally going to be unique to each individual. Some annual costs that could be incurred for health purposes include Medicare premiums, supplemental insurance policy premiums, and any out of pocket expenses for uncovered events or items.





The following long-term care statistics come from the National Association of Insurance Commissioners [5]:

- 52.3% of people turning 65 who will have a long-term care need during their lifetime
- 46.7% of men turning 65 expected to have a long-term care need during their lifetime (this number rises to 57.5% for women!)
- 22% probability for men of needing more than one year in a nursing home (36% for women)

These odds are high enough that it is a **MUST** have conversation and an extremely important part of the planning process. Generally this is modeled by either planning to have long-term care insurance to cover all or most healthcare needs, or by modeling one or multiple hypothetical health events over the course of retirement [2]. Either way, it is important to plan for a long-term care need.



# Impact of Taxes

Many asset withdrawal decisions made by pre-retirees and retirees are affected by income taxes. Ideally, the planner should help the client target the appropriate income tax bracket. Managing the income tax brackets helps the client choose whether to draw funds from a taxable account, a tax-deferred account, or a Roth IRA account. For example, if the client has low taxable income years early in retirement with the expectation of higher taxable income in later years, he or she may consider a Roth IRA conversion. Taxes can have a major impact on the success of the plan, so an effective tax strategy should be modeled and implemented.







## Conclusion

At its core, cash flow analysis is an important exercise for an individual that wants to maximize their chances of making it through retirement the best standard of living as possible. Modeling cash flows to simulate retirement is a dynamic tool for flexible retirement planning to help people achieve their life goals, so comparing actual results over time to projections can help adapt the plan and make it more accurate. Knowing an individual's cash-flow-needs and timing will help you plan to set more money aside or use money from investments to get through lean times if needed. Understanding the concept of cash flow helps determine minimum income and liquidity need. After analyzing cash flow, an advisor can discuss proper allocation and time frame. Maintaining positive cash flow can help a person maintain happiness through retirement.



## Sources

Brooks, Rodney. "Alternatives to Long-Term Care Insurance." U.S. News & World Report, U.S. News & World Report, 26 July 2019, [money.usnews.com/money/retirement/aging/articles/alternatives-to-long-term-care-insurance](https://money.usnews.com/money/retirement/aging/articles/alternatives-to-long-term-care-insurance).

[1] <https://seekingalpha.com/article/4186342-projecting-retirement-cash-flow>

[2] <https://www.thetaxadviser.com/issues/2015/dec/planning-for-cash-flows-in-retirement.html>

[3] <https://www.thebalance.com/retirement-income-vs-cashflow-vs-withdrawals-2388886>

[4] [https://news.gallup.com/poll/234032/social-security-financialbedrock-retirees.aspx?g\\_source=link\\_NEWSV9&g\\_medium=TOPIC&g\\_campaign=item\\_&g\\_content=Social%2520Security%2520Still%2520Financial%2520Bedrock%2520for%2520Retirees](https://news.gallup.com/poll/234032/social-security-financialbedrock-retirees.aspx?g_source=link_NEWSV9&g_medium=TOPIC&g_campaign=item_&g_content=Social%2520Security%2520Still%2520Financial%2520Bedrock%2520for%2520Retirees)

[5] [https://www.naic.org/documents/cipr\\_current\\_study\\_160519\\_ltc\\_insurance.pdf](https://www.naic.org/documents/cipr_current_study_160519_ltc_insurance.pdf)

## Disclaimer

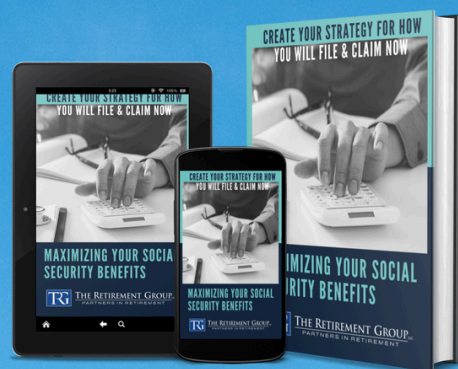
Past performance cannot guarantee future results. Investing involves risk including the potential loss of principal. Current performance may be lower or higher. No investment strategy can guarantee a profit or protect against loss in periods of declining values. Please note that individual circumstances can vary. Therefore, the information presented in this letter should only be relied upon when coordinated with individual professional advice.



**For more Financial information,  
check out these resources...**



**Lump Sum vs.  
Annuity**



**How to Maximize Your  
Social Security Benefits**



**Disclosure: Advisory services offered through Wealth Enhancement Advisory Services, LLC, a registered investment advisor and affiliate of Wealth Enhancement Group®. Wealth Enhancement Group is a registered trademark of Wealth Enhancement Group, LLC. Trust services offered through Wealth Enhancement Trust Services, LLC, a trust company chartered under South Dakota law.**

**Check the background of investment professionals associated with this site on the [Investment Advisor Public Disclosure website](#).**

**WEAS ADV Part 2A with Form CRS Form CRS WEAS ADV PART 2A Appendix 1**

**This site is published for residents of the United States only. Investment Advisor Representatives of Wealth Enhancement Advisory Services may only conduct business with residents of the states and jurisdictions in which they are properly registered. All information herein has been prepared solely for information purposes, and it is not an offer to buy or sell, or a solicitation of an offer to buy or sell any security.**