Chapter 8

HOW TO RETIRE ON TIME AND STAY RETIRED

"There's no such thing as bad weather, only unsuitable clothing."

– Alfred Wainwright

By this point, you should have a Kedrec Wealth Plan™ that is close to where you want it. You should also have a rough idea of how to fund your retirement portfolio, based on your plan. Your plan should be a reflection of your lifestyle and legacy goals. The last question to answer is, what do you do once the plan and portfolio are funded?

This chapter is intended to help you understand how to maintain your plan. As I mentioned before, I honestly believe that with the right plan, supported by the right strategies and portfolio, most people should be able to manage their retirement on their own. It's time to show you how to manage your plan and portfolio so regardless of market conditions, you can keep income coming in without accentuating your losses.

THE KEDREC WEALTH PLAN™ INCOME PLAYBOOK

How you manage your assets will change over time. For example, when you first retire, IRA to Roth conversions may be more important to you than when you are in your late 70s. Each income play has its place. If markets are down, you take income from your Kedrec Reservoir™. If markets are up, pick one of the plays to execute, based on your goals.

Ready?

Let's begin.

The Max Tax Play

The Max Tax Play is what I call it when you set a max tax amount, take 100% of your income from pre-tax accounts, and use the rest as IRA to Roth conversions. The idea here is to basically set a limit or maximum amount of pre-tax distributions for one year or multiple years. Instead of maxing out your bracket, you set your max limit on your terms. We will go through a simple tax assessment later in the book. For now, try to learn the universal rules behind the strategies.

Let's say, for example, your max limit is $150,000 and you have an effective tax rate of 20%. That means you would expect to pull $150,000 from pre-tax accounts for one year or several years, pay around $30,000 in income tax, and then split between how much your income is and how much you can convert. Here's an oversimplified breakdown to try and help illustrate this play.

Year 1:

- Max Tax: $150,000
- Taxes: $30,000
- Net Income: $100,000
- Net Conversion: $20,000

"Net Conversion" means the amount, after taxes are paid, that actually went into the tax-free account (e.g., Roth IRA).

Year 2:

- Max Tax: $150,000
- Taxes: $30,000
- Net Income: $102,000
- Net Conversion: $18,000

Year 3:

- Max Tax: $150,000
- Taxes: $30,000
- Net Income: $105,000
- Net Conversion: $15,000

Hypothetical example shown for illustrative purposes only.

The theory behind this play is to determine how much you are willing to pay in taxes over the next few years. Now you know what you can roughly expect each year while you enjoy your income and convert the leftovers from pre-tax accounts to tax-free accounts. This means you pay taxes on the converted funds now so that they can be accessed tax-free later in retirement. Do not start this until after age 59 ½. You do not want to pay additional penalties by taking funds out incorrectly before the age of 59 ½.

The play is usually more appropriate when current tax rates seem like they will be lower than in the near future. Typically, this strategy would be used between when someone retires and the age of 65 (before they file for Medicare). If you are 65 or older, make sure you watch out for the Medicare Income-Related Monthly Adjustment Amount, or IRMAA. When you take too much income from taxable sources, you can trigger an increase in your Medicare Premiums.

Typically, this strategy can be used to help minimize future tax burdens fast.

The Minimalist Play

The Minimalist Play, as I call it, only works once you have converted enough of your assets from pre-tax accounts to tax-free accounts. This play typically shows up later in your plan.

To execute this play, you will first determine how much pre-tax income you can take without putting yourself into the next tax bracket. That includes your Social Security benefit, your pension (if you have one), and any other income stream that may trigger taxes. Once you have established your taxable income limit from pre-tax accounts, you then take the rest from your tax-free accounts.

Some people will be able to implement the Minimalist Play within the lowest tax bracket, depending on their Social Security benefit. Those who have pensions or other taxable income streams may find themselves in the second or third lowest tax bracket when implementing this play, and that's okay. This play can vary significantly, based on your unique situation.

The Buffet Play

I'm not talking about Warren Buffett. I'm talking about a literal buffet, like where you'd go for lunch or dinner. When you arrive, it's hard not to take a little bit of everything, right? The purpose of this play is to take income from sources that need to be brought back into harmony with your lifestyle and legacy goals. Sometimes, accounts can grow faster than expected. Other times, tax and other financial regulations may change. Flexibility, as long as it is based on a system that guides your decisions, can be a huge benefit.

Depending on the growth of the accounts, tax rates, current market conditions, and so on, you may decide to take more or less from certain accounts based on current tax conditions. Maybe you want to focus on taking income from pre-tax accounts because your Required Minimum Distributions

(RMD) may become an issue. Maybe you decide to take more income from your reservoir because it is getting too big.

As long as you let your lifestyle and legacy goals drive your decisions, and you never ignore the universal rules of retirement that were discussed in this book, you should be able to dynamically manage your plan based on the ever changing environment.

HOW TO STAY RETIRED EXERCISES

When a kid gets their driver's license, it means they have proven to the DMV that they know how to drive, technically speaking. That doesn't mean they are any good at it. It means they understand how to start a car and get from point A to point B with a reasonable chance of not crashing. There's something to be said about having "time in the saddle." The same could be said about managing your plan and portfolio.

We've covered the universal rules, framework, and strategies enough to be considered dangerous. Now, it's time to put them to the test. Consider the rest of this chapter your driver's test. Let's run a few hypothetical scenarios to see if the universal rules in retirement make enough sense that you would be able to correctly apply them.

Please note that even if you pass this casual test, remember, it's okay to still be a little nervous. Admittedly, it could take years of time in the saddle before you start to feel comfortable managing and maintaining your plan and portfolio.

Let's begin.

Scenario 1: The market crashes 35% in the second year of your retirement. Where do you pull your income?

Answer: You would pull your portfolio income from the Kedrec Reservoir™. After a year has passed, you verify whether or not your accounts have recovered. If they did recover, then all would be well, and you could pull income from anywhere.

If your other accounts did not recover, as was the case for many in 2000, 2001, and 2002, then you would keep taking income from your Kedrec Reservoir™ so that you don't compromise your other accounts. Remember, you don't want to accentuate your losses.

Scenario 2: You're turning 65 years old and you still have a significant amount of money in pre-tax accounts. Do you keep converting the maximum amount of Traditional IRA assets to Roth IRAs while staying within your current tax bracket?

Answer: The answer is it depends. However, as a general rule, once you turn 65, you want to keep your income tax as low as possible so that you don't increase your Medicare premiums. Consider setting your Max Tax Play limit just below IRMAA, if possible.

Scenario 3: The market had an incredible year. Where should you pull your income?

Answer: This is a trick question. You can pull income from any investment group. However, when markets have been up, it is generally more efficient to pull income from different accounts in order to help minimize future tax liabilities. This means it may be in your best interest to pull from your risk accounts and your reservoir. Also, you may want to pull from your pre-tax accounts and your after-tax accounts to help minimize your overall tax burdens. It's a balancing act to maximize income while trying to keep tax liabilities low.

Scenario 4: My accounts have done well for the past few years. I want to spend as much as I can since I don't plan on leaving anything to my kids. Can I increase my income?

Answer: Over the span of five to ten years, it is expected that some years may exceed expectations while other years may underperform. Subtle adjustments after five years or so may be appropriate. Anything less than five years may not be appropriate.

If you start with two good years, and then increase your income, you may be spreading yourself too thin when you get to the third year. If the third year lacks sufficient performance, it could really hurt your plan. Do not get greedy. Stick to the plan and expectations that were originally set. Most of all, maintain the necessary liquidity in your Kedrec Reservoir™.

Scenario 5: I've been retired for ten years now. My Kedrec Reservoir™ has gone down significantly. Should I put more into my reservoir?

Answer: It's hard to offer a definitive answer, but as a general rule, it is okay to have less in your reservoir over time. Your risk accounts are expected to eventually dwarf your reservoir.

One of the few times you may consider putting additional assets in your reservoir would be if you have been pulling income from them exclusively over the past few years due to poor market performance. This could happen if you were to retire at the beginning of a flat market cycle.

Scenario 6: How often should I review my estate plan?

Answer: It is a good idea to have your estate plan reviewed and updated every two to three years. Laws change. If your estate plan is not updated, it may lead to discrepancies that prevent your intentions from being fulfilled.

Scenario 7: I'm getting bored in retirement. What should I do?

Answer: Get a part-time job. Go volunteer. Find religion. If single, consider dating. Search until you find purpose. You must have a reason to get up in the morning. If you don't, research shows that you will cognitively decline at a faster rate.

Unless you have a purpose in retirement, it may not be worth it. The "vacation" honeymoon phase of retirement usually only lasts a year. Once the honeymoon phase is done, depression can set in. Do not let that happen to you.

Many people reinvent themselves in retirement. Do whatever it takes, but find purpose. Retirement is meant to be a good time, not a lonely time.

In Conclusion

As I wrap up this chapter, I want to invite you to consider other scenarios that may concern you. There are an infinite number of situations that can cause you to lose sleep. Dwelling on them with a spirit of procrastination won't bring you peace. You'll need to take action in order to find a solution. Running through those situations now can help you be prepared for if or when they happen. Keep doing these exercises until you feel confident about the idea of retirement. Remember, your retirement is for you. Don't retire for someone else.