Practical Planning, Thought Leadership & Best Practices for Retirement Planning
By Lyle Benson, CPA/PFS

Although CPAs work with their clients on a broad range of issues, retirement planning is a critical piece of any CPA's practice—and even more so for those who offer financial planning services. These accounting professionals, many of whom also have the Personal Financial Specialist (CPA/PFS) credential, need to understand how to help their clients plan for the kind of retirement and lifestyle that suits them.

Topics ranging from savings and cash flow considerations to investment planning, Social Security and even the impact of divorce, among others were covered in 2015, beginning with AICPA's Thought Leadership Panel held during the 2015 Advanced PFP Conference. Here is a summary of those discussions.

Special thanks to our 2015 Thought Leadership Panel for participating in this session, providing valuable insights and creating resulting deliverables throughout the year: Lyle Benson, CPA/PFS, Jean-Luc Bourdon, CPA/PFS, Gina Chironis, CPA/PFS, Dirk Edwards, CPA/PFS, Michael Goodman, CPA/PFS, Charlie Kowal, CPA/PFS, Lori Luck, CPA/PFS, David Oransky, CPA/PFS, Ted Sarenski, CPA/PFS, Jim Shambo, CPA/PFS, Scott Sprinkle, CPA/PFS, Tracy Stewart, CPA/PFS, David Stolz, CPA/PFS, and Tom Trainor, CPA.

Envisioning and Defining Retirement
Although the plan and solutions to achieve retirement goals vary greatly from client to client, CPA financial planners have a unique perspective, knowledge and credentials to help their clients understand their current and future spending, assess their goals, and better plan for their future and retirement.

"Don't wait until clients are in their late '50s to begin discussing retirement planning," says David Oransky, CPA/PFS, principal and founder of Laminar Wealth in St. Louis, Missouri. "From the very beginning of the relationship, start asking them what they envision their life looking like and what's most important to them. Not only will this help clarify their goals and enable you to plan more effectively, but you're also more likely to be able to help them start living that life much sooner than traditional retirement age."

Oransky believes CPA financial planners can help clients plan for retirement by helping them understand risk, focus on cash flow and optimize asset location within a portfolio.

First, clients need to understand the difference between true risk and market fluctuations. This will allow advisers to build portfolios that minimize the risk of a client not reaching his or her goals, or living the life they want.

"Investors with more resources than they need may be able to confidently reach their goals while having little volatility in their portfolio if, for example, they first build a liability-matching bond ladder of treasury inflation-protection securities," says Oransky. "However, for many investors, this level of security isn't an option. Instead, they'll need to accept moderate fluctuations in their portfolios in order to minimize the risk of outliving their money."

It's also important to focus on cash flow. Many retirees who are concerned about having sufficient income allocate much of their portfolio to higher-yielding bonds, as well as higher-yielding or dividend-paying stock, by extending the credit quality and term.

"Retirees don't need income; they need cash flow," says Oransky. "Cash flow can be derived from income and by harvesting capital gains. Instead of focusing on income, planners should focus on total return when constructing a portfolio. This allows you to better focus on diversification and after-tax return."

Oransky also cautions against overlooking tax-planning opportunities during portfolio construction.

"CPA financial planners have the knowledge and credibility to implement these strategies more effectively than other planners," he says. "The process should start when constructing model portfolios and choosing funds. For example, choosing all-in-one funds may limit the ability to effectively locate assets in different account types based on tax characteristics. Instead, a more "slice-and-dice" approach allows for maximum asset location potential."

Savings and Cash Flow Planning Insights

As Oransky says, having enough cash on hand is a significant focus for retirees. The consensus among the panel was that CPA financial planners should take the time to analyze a client's cash flow, while offering practical solutions to ensure liquidity.

"Since spending is one of the few aspects clients can control during retirement years, it's important that you sit down and discover what they are actually spending," says Lori Luck, CPA/PFS, of CLS Financial Advisors, Inc. in Portland, Oregon. "This will not only create a learning experience for the client, but also allow both of you to see the big picture by being able to more easily identify and implement changes in the future."

Realistic expense information to estimate future cash flows is absolutely necessary, says Luck, and there are several ways to gather this information: ask clients to estimate a specific annual amount they expect to spend in retirement, complete a detailed pre-printed form with expense categories and information detailed, or obtain information directly from their personal bookkeeping software reports.

"Once you have the information you need, you are able to provide feedback to your clients on how to save," she says. "One example for managing cash, after calculating monthly cash needs, is for the client to establish a recurring monthly deposit of a fixed amount into separate bank accounts for discretionary and non-discretionary expenses. This can help clients determine if they are staying within their budget. Setting aside cash each month into separate accounts for travel and targeted gifts can also help manage expenses that are annualized."

Another area of concern for cash flow is estimating income taxes. Luck says there are many tax-triggering events and decisions to make that happen before and after retirement that you must plan for, including but not limited to retirement plan rollovers versus lump sum distributions, employer stock in retirement plans, delaying Social Security benefits to age 70, and taking cash distributions from other accounts to make up for delayed Social Security benefits, either from retirement accounts or taxable accounts. The adviser needs to prepare tax projections over a period of at least 10 years, in many cases, to analyze the income tax impact of these types of decisions over a multi-year period.

She also offered insight on several other factors to consider when it comes to saving and planning for retirement:

- **Housing costs and decisions:** Own a home with living costs in mind, rather than as an investment. Often, the family home is so much a part of a client's identity that it can be too difficult or drastic to make a transition. The plan may be to show them early on that they can no longer afford their family home and need to downsize. In addition, advise your clients not to purchase a home unless they plan on staying for at least 5-7 years, and make sure they understand the tax advantages of owning versus renting.
- **Rising healthcare costs:** Plan on increased healthcare costs, including potential long term care, in your clients' financial plans.
- **Entitlement issues:** Find out the answers to these questions: How long will your clients be supplementing their children's income? How are your clients going to plan for adult children possibly moving back home after college? How can you help clients teach their children to become financially independent?
- **Legacy and philanthropic goals:** Look at how your clients can use appreciated assets in charitable planning. Can your clients afford to give more during life, as opposed to at death? How should you incorporate life insurance?

"It's very important to check in with clients over time to compare actual spending to planned spending, and give them feedback on how they are doing so that they have the ability to modify spending habits they can control during their retirement years," she says. "Sometimes, we have to have hard discussions with our clients to help them be realistic about their future."

Safe Withdrawals and Evaluating Simulation Techniques

Creating a safe withdrawal policy is another key component to retirement planning, and while your clients probably do not want to get into the technical details associated with safe withdrawals, it's important for planners and advisers to be up to speed on this topic.

Jim Shambo, CPA/PFS, heads up Lifetime Planning Concepts in Colorado Springs, Colorado, and is author of *The CPA's Guide to Practical Retirement Planning* (available with PFP/PFS membership and for-sale for non-members). One of the simulation techniques he covers in the guide—and discussed at the Thought Leadership Panel—is Monte Carlo, a productive algorithm for yielding results.

"It's paramount that you view Monte Carlo as a compass, not a GPS," he says. "A tool that only measures portfolio balance, while ignoring client behavior, can't accurately pinpoint real-life success rates. Otherwise, you are doing your client an injustice."

Shambo advises that planners ought to document the withdrawal plan in a policy statement that acknowledges the uncertainties, plans for actions to react to bad events and avoids any predictions of success rates. This is accomplished by avoiding the predictive success rates generated from Monte Carlo and focusing, instead, on running stress tests and what-if scenarios.

"Run stress tests on the most common non-client reasons failure occurs, such as economic and market variables that identify weak points in a withdrawal plan," he says. "As part of your strategy, stress test different inflation rates, the first 10-year portfolio returns that result in spikes in withdrawal rates that are 20% greater than the initial rate, and early year portfolio losses."

Shambo also says to run "what if" scenarios on the most common client-related failures, including excessive withdrawal, failure to stay the course on asset allocation and excessive healthcare costs.

"Use the knowledge gained from these activities to explain to clients the risks they face and the tools you will use to address the weak points," says Shambo. "This process allows for a more solid withdrawal plan, but remember it is the job of the planner to consider each client's individual needs and behavior."

Shambo offers several key areas to look at when monitoring and adjusting the plan over time:

- Compare annual withdrawal rates to the initial withdrawal rate to identify excessive withdrawal patterns, using Guyton decision rules or the Vanguard floor and ceiling rules.
- Prepare a Withdrawal Policy Statement (WPS) that identifies when changes will be required in the client's annual withdrawals (a sample WPS is included in *The CPA's Guide to Practical Retirement Planning*).
- Meet with clients to review the WPS and reinforce the changes needed as they occur.
- Discuss healthcare changes that could impact future cash flow needs.
- In the event of death or divorce, restart the entire planning process.
- Spending inflation is a behavioral issue, rather than a mechanical annual raise based on the Consumer Price Index (CPI)—and it should be personalized. Some clients are spendthrifts and others frugal; these behaviors override the CPI-based spending inflation used routinely in withdrawal studies.
- Income taxes and portfolio expenses are not considered in the withdrawal studies. Help clients minimize both, but you also need to include estimates of both of these costs in any projections made.

To wrap up the safe withdrawal discussion, Shambo says planners may have questions as to whether the 4% rule still works. The 4% rule represents a rough calculation that did not consider the uniqueness of each client and many other real world facts.

"Planners will want to look at the pros and cons," he says. "For example, the rule uses constant inflation adjusted spending when dynamic spending will be required for most portfolios over most periods, especially in times of portfolio stress. In addition, the rule does not personalize clients' spending behavior, but rather, assumes all clients increase spending based on the Consumer Price Index."

The Impact of Divorce on Retirement Planning

We've all had clients who divorced, only to find the spouses sometimes ill-equipped to deal with retirement planning, especially when it comes to cash flow and investments.

"It is not unusual for divorcing women who are 50+ years old to feel ashamed that they did not keep up with the family finances throughout their long marriage," says Tracy Stewart, CPA/PFS, CFF, owner of a practice that specializes in collaborative divorce. "However, retirement planning is an excellent starting point for their education because they are scared about their long-term financial security, regardless of the size of their wealth."

Whether your client is male or female, clients who are going through later-life divorce need help in a number of areas, especially when it comes to figuring out how to navigate the complicated maze of their retirement accounts and division of assets. Stewart says there are three conditions of the retirement account related to vesting and maturity:

1. Non-vested and non-matured occurs when the employee has terminated and only has rights to the amount of his or her contributions to the plan, plus interest.
2. Vested and non-matured occurs when the employee is terminated, but can receive some benefits beyond his or her contributions.
3. Vested and matured occurs when the employee is terminated, and he or she is currently entitled to certain benefits that are in addition to amounts previously contributed.

She says the first issue in splitting a retirement asset is whether the asset itself will be divided or offset with another asset.

"Some retirement accounts cannot be divided," she says. "A couple or a court may decide to offset a retirement account with other asset(s). When the other assets are not subject to future taxes, you can estimate any future taxes on the retirement accounts. This levels the playing field when offsetting non-retirement assets with retirement assets."

When the retirement account is to be split, a Qualified Domestic Relations Order (QDRO) might be needed. QDROs are court orders directed to a retirement plan administrator to pay benefits to the alternate payee. QDROs are used for qualified plans, including a 401(k), 403(b) and pensions. These plans are subject to ERISA rules, which have an anti-assignment clause. To get around this clause, a QDRO is used to divide the retirement benefit. QDROs also enable these plans to be divided without tax consequences. QDROs are not required to divide IRA accounts.

"Clients in later-life divorces will not have enough time to rebuild their retirement assets," says Stewart. "They are grateful for the advice CPAs can provide regarding their options for dividing their retirement accounts."

Social Security in the Context of the Full Retirement Picture

CPA financial planners need to help their clients plan for Social Security benefits, and there's no doubt that clients under a certain age are asking whether Social Security benefits will be available when they are ready to claim them.

Addressing this on the panel was Ted Sarenski, CPA/PFS, CEO and president, Blue Ocean Strategic Capital, LLC, in Syracuse, New York. Sarenski is author of *The CPA's Guide to Social Security Planning*, another publication available with PFP/PFS membership and for-sale to non-members.

"By 2033, the Social Security Administration estimates there will be enough money to pay out 75% of expected benefits, so even if Congress does not act to remedy the shortage, retirees will only lose out on 25% of their benefits—and that's a worse-case scenario," says Sarenski. "Social Security benefits won't disappear completely, so it's up to planners to advise their clients on how to plan for this 25% shortage."

The Social Security Administration estimates that 3.9 million people will turn age 62 in 2015 and another 4 million will turn 62 in 2016. In 2014, the average age of men applying for Social Security retirement benefits was 64.4; it was 64.2 for women. If planners deal with high-net worth clients, Sarenski says Social Security isn't as important because the clients will have a larger pool of money. However, if clients have a more modest income, then these benefits become even more important.

"What they want is the highest check possible as soon as they can get it, but because people are living longer, we advise the higher wage earner to wait until age 70 to begin claiming benefits," he says.

Because it's likely that one or both spouses may live until age 95, Sarenski says that if clients want to claim Social Security at age 66, they'll actually receive more of their benefits to live on if they can wait until they get older. Planners need to be aware of other issues as well. For example, while file and suspend is normally associated with married couples, single people can also voluntarily file and suspend at full retirement age.

“Let’s say you find out at age 68 that you have a terminal illness; you can go back to age 66 and get all that back pay and the monthly benefit you would have gotten at that age,” says Sarenski.

Sarenski and other panelists urged planners to help their clients plan conservatively for Social Security benefits, but remain realistic that if Social Security isn’t included in a financial plan at all, planners could be forcing their clients to work longer and they may never retire.

“Social Security is an important piece of everyone’s retirement, so it’s important that retirees maximize those benefits when they can,” says Sarenski. “It’s also the only annuity that gives you inflation protection.”

Investment Planning Insights in Retirement

Of course, CPA financial planners will want to ensure their clients are comfortable with their investments. Any investment discussion includes evaluating a person’s risk tolerance and capacity, matching client assets and cash flow with spending, and several other factors.

First up is evaluating a client’s risk tolerance. According to panelist Thomas J. Trainor, CPA, managing director of Hanover Private Client Corporation in Toronto, Ontario, risk tolerance is broken down into two parts: financial capacity for risk and emotional capacity for risk.

“Determining a client's financial capacity for risk is essentially a very mathematical exercise,” he says. “It is a function of asset and income requirements, as well as the amount and nature of the assets. On the other hand, emotional tolerance for risk is much harder to judge. While questionnaires and the use of professional judgment are frequently used, it is still very hard to assess client risk tolerance given that risk tolerance is frequently a function of the time environment we are in; a client’s emotional risk tolerance changes with the market conditions.”

While the financial capacity for risk is basically a function of the client's numbers, Trainor says emotional tolerance for risk can be modified successfully over time by educating the client. As a result, if a planner has clients who are very risk averse, he says to educate them over the long term in order to move them to a more rational view of risk.

When matching client assets and cash flow with spending, Trainor says to make sure you dedicate certain assets based on volatility within the timeframe in which they are required. This allows you to look specifically at the client's portfolio and the net of any pensions or other types of annuities that they may have.

For example, if it is expected that a client will spend approximately $10,000 per month in retirement, but has an indexed pension of $3,000 per month, the net demand on the portfolio will be $7,000 per month, and that is the amount used to structure the portfolio.

“Let’s look at spending in 5-year increments; in 10 to 15 years, start to introduce equity for those components of the portfolio,” says Trainor, “The reason why we wait that long is that there is a minimal chance of a negative return if you hold an equity portfolio for that period of time. As you move through time, rebalance the portfolio and add up the individual tranches to determine the overall asset mix.”

Another factor to consider in investment planning is what Trainor refers to as “human capital,” or the amount of income a client can generate in his or her lifetime. In addition, the nature and type of employment income will directly impact how a portfolio should be structured.

“A surgeon or tenured professor will have very stable income regardless of economic conditions, while a commissioned sales person may see his or her income, and employment opportunities vary widely with fluctuations in the economy. This will directly impact the level of risk that the individual can take in the portfolio.”

What is unique about all jobs, whether you are self-employed or an employee of a large company, are the human factors of morbidity and mortality. “In order to have a complete assessment of the characteristics of the employment income, you have to make an assessment of the human factor risks,” he says.

Integrating Tax and Retirement Planning

All clients want to minimize their tax liability as much as possible. CPA financial planners can work with their clients to help them understand the various strategies they can use so that the golden years are just that, golden.

“Tax planning strategies for retirees should consider hedging against higher future tax rates for seniors with income from Social Security, investments and required minimum IRA distributions,” says Gina Chironis, CPA/PFS, CEO of Clarity Wealth Management. “For example, where future tax brackets are expected to be the same or higher, there are multiple Roth conversion and Roth recharacterization strategies that can reduce the negative impact of future taxes.”

A few of these strategies include the following:

- Optimal Roth conversion strategy for retirees. Convert while in lower tax brackets immediately following retirement, before Social Security income and/or required minimum IRA distributions begin at age 70 ½. This could be done in one year or spread out over multiple years.
- Double conversion. Convert 2x the desired amount in January, with 50% in equities in one Roth IRA and 50% in fixed income into a second Roth IRA. This allows the flexibility to recharacterize the first IRA if the equity value goes down, as well as the ability to recharacterize the second IRA if the equities go up.
- Establish multiple Roth accounts and convert each unique asset class or investment type in the Traditional IRA to a unique Roth account. This is done to take full advantage of recharacterization opportunities. For large IRAs, the rewards of this approach could be worth the complexity, since the more Roth accounts that are established, the greater the flexibility in recharacterization.
- Locate tax inefficient and highest growth potential assets. This includes emerging markets, international equities and REITs, inside the Roth IRA, once converted.

“For the greatest impact, tax planning strategies should be integrated with cash flow modeling and viewed over a 15 – 20 year time horizon,” says Chironis.

The Value of the CPA Financial Planner in Retirement Planning

Although non-CPA planners can implement these and other strategies, your credibility as a CPA financial planner or CPA/PFS – with the powerful combination of extensive tax expertise and comprehensive financial planning knowledge—should put you head and shoulders above others when it comes to offering integrated retirement, tax, estate, risk management and investment advice. Educate yourself, first, on financial planning issues and solutions, then meet with your clients to help them create impactful, life-changing plans.

Resources from the AICPA Personal Financial Planning Section

The AICPA PFP Section offers a robust suite of retirement planning resources to PFP Section members, inclusive of CPA/PFS credential holders, at aicpa.org/pfp/retirement, including:

- *The CPA's Guide to Social Security Planning* (free excerpt available to non-members)
- *The CPA'S Guide to Financing Retirement Healthcare* (free excerpt available to non-members)
- Archived retirement webcasts and materials
- Retirement planning content from Forefield Advisor, a premium, web-based client communication and education tool
- Safe withdrawal, Roth conversion, long-term care resources, and more
- Retirement learning included in the PFS Program

Deliverables that resulted specifically from this 2015 dedicated effort can be found here and include the following (with the exception *The CPA's Guide to Practical Retirement Planning* that is included with PFP/PFS membership, these resources are open to all):

- *The CPA's Guide to Practical Retirement Planning* (free excerpt available to non-members)
- The three-part 2015 webcast series on practical retirement planning, which features many of the panelists quoted in this article
- A video series featuring retirement planning insights from leading CPA financial planners
- Articles and blog posts
- Media Advisory Board surveys and results

Lyle Benson, CPA/PFS, is founder of L.K. Benson & Co. P.C., in Baltimore, Maryland. He is immediate past chair of the AICPA's Personal Financial Planning Executive Committee.