WEALTH INVESTMENT PROSPERITY RETIREMENT PLANNING FOR AGE GAP COUPLES

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Planning for retirement is tough enough for couples who are roughly of equal age. Couples whose ages differ more widely face additional hurdles, writes Mark Bechard. One of the biggest challenges facing financial planners when advising clients about retirement is getting them to appreciate how many years they will spend in retirement and, as a result, how long their retirement capital will have to provide an income.

If you're married and there is a significant difference between your and your spouse's age, this will extend your retirement funding requirements. "I struggle to get my clients who retire at 65 to appreciate that they will need an income until they are 100. If a man retires at 65, he has to fund about 35 years in retirement. If his wife is 10 years younger than him when she retires, she has to fund 45 years in retirement," says Janet Hugo, a director of the Sterling Group and the 2018 19 Financial Planner of the Year. Typically, one spouse is older than the other and will retire first, so when does the difference in age become a significant factor in retirement planning?

Mark MacSymon, a wealth manager at Private Client Holdings and the 2017 / 18 Financial Planner of the Year, says that, as a "rule of thumb", it is when the age gap is 10 years. However, he points out that "a number of idiosyncratic characteristics determine whether or not the age gap does, in fact, have a significant bearing on a couple's successful retirement". These include the health status of both partners, whether the older or younger spouse is the primary income generator, and whether they will have sufficient capital to meet their income requirements based on the life expectancy of the younger spouse. The sooner an age gap couple seek professional financial advice about their retirement, the better.

The optimal solution is to establish how much capital they need to accumulate by the time each partner reaches retirement age and to save accordingly. Staggered retirements depending on the dynamics of the relationship, there can be financial and psychological advantages if one spouse retires earlier than the other. The younger spouse can continue to earn an income, taking the pressure off the family's draw down of retirement capital. And there will be a tax benefit if the working spouse continues to contribute to a retirement fund. Second, instead of both spouses having to adjust to retirement more or less simultaneously, one spouse can continue with a normal working life while the other gets used to not working.

However, Hugo and MacSymon say that retiring at different ages can place a strain on the relationship. The retired spouse may want to travel, or move to a retirement village or a sedate seaside town, whereas the younger spouse could still be at the peak of his or her career. The working spouse could feel resentment towards the retired spouse if she it's invariably the wife is putting in long days at the office while the retired spouse "is sitting around at home" and still expects the working spouse to do household chores.

A financial planner can provide guidance with respect to the emotional and psycho logical challenges associated with this transition. "Communication and.com promise are key ingredients for a successful transition but from the financial planner's lens, offering recommendations and solutions about what has worked and what has not in similar situations can help provide answers," says MacSymon. "I have a family whom I advise that has an eight-year age gap. The wife continues to work as a psychologist and the husband is a retired doctor. The tenuous balance at this stage is more around how and where their time is spent in that the wife is excelling within her practice while the husband is looking to exit the pace of Cape Town." Retirement plan as income sustainability is linked to longevity,

Hugo and MacSymon say the retirement plan should be based on the partner with the longest life expectancy, which, in the overwhelming majority of cases, means the forecast is based on the life expectancy of the wife. Says MacSymon: "In scenarios where income and capital available from accumulated assets are likely to become completely exhausted based on a forecast period determined by the spouse with the longest life expectancy, we make suggestions about ways to extend the longevity of capital. This might include suggesting that the older spouse delays retirement for as long as possible to defer the drawdown of retirement savings but we may also suggest a semi retirement strategy or a lower income drawdown.

Depending on the dynamics of the relationship, there can be financial and psychological advantages if one spouse retires earlier than the other monthly levies. Once the cash flow requirement has been determined, Hugo says retirement capital should be invested using a time weighted, or liability matched, investment model. This means constructing an investment strategy that will ensure sufficient funds are available to meet each year's drawdown needs. The money that will be withdrawn over the next two to three years should be invested in low risk money market or income funds. Capital that will be needed to fund income requirements in five or six years' time should be in moderate risk investments, such as balanced funds, while capital that will be needed in seven or more years should be in high risk equity funds.

Hugo says the time weighted investment model ensures that near term cash requirements will be funded from conservative investments. "It means that my clients don't have sleepless nights and phone me up experience, cash flow models that help clients to attribute value to the decisions, such as working two or three years longer, or working part time as part of a semi retirement strategy, are particularly empowering. They put both the planner and the family firmly in control of how best to smooth resources over their planned retirement. In the absence of such planning models, and especially when a large age gap exists between spouses, decisions to take early retirement or to prematurely sell a business are akin to a guessing game with punitive consequences." Hugo says the key to dealing with the longevity challenge exacerbated by an age gap is to base the retirement plan on the couple's annual cash flow needs in retirement. This exercise requires a detailed examination of the couple's expenses and lifestyle aspirations. She says the common assumption that there will be a significant decrease in expenses in retirement is not borne out by reality.

At best, expenditure will remain the same although savings will be accrued by not travelling to and from work or eating out during lunch, healthcare expenses tend to increase markedly as one gets older. She says another false assumption is that downscaling to a smaller home or moving to a retirement village will result in a big saving and unlock a large amount of capital. An apartment in a sectional title scheme or a cottage in a retirement village may be smaller but it will not come cheap plus this type of accommodation charges every time the market wobbles." It also overcomes the common mistake made by many retirees: investing all their capital too conservatively because they fear they will lock in their losses if they have to drawdown when equity markets are in a slump. Life or living annuity? With the extended longevity challenge in mind, which pension is better: a living annuity or a life guaranteed annuity?

MacSymon says that, in general, if there is little likelihood of a couple exhausting their retirement capital, under even the most conservative of assumptions, a living annuity is the default option. "These instruments need to be managed with care, and the combination of the income drawdown selected and asset allocation decision are the key drivers of the instrument's success." If, on the other hand, uncertainty about the longevity of capital is a concern, transferring that longevity risk to an assurer via a life annuity would be the better option. "If the writing is on the wall and the likelihood is high that retirement capital within a living annuity will be exhausted during the younger spouse's lifetime, switching to a life annuity sooner rather than later is preferable. If this decision is unnecessarily delayed, it is probable that the family or the surviving spouse will need to adapt to a much lower income derived from the life annuity, which will result in a difficult lifestyle shift that'll take some getting used to. The longer the delay, however, the more difficult the adjustment. The availability of additional discretionary capital and existence of passive income for instance will influence this decision."

Another solution, he says, is to split retirement capital between the two types of pension, with a life annuity ensuring there is sufficient income to meet "essential" expenditure while a living annuity caters for "nice to haves". "Whether a life or living annuity, or a combination thereof, is employed, the answer ultimately depends on the couple's unique circumstances. But for those couple's where a large age gap exists, a life annuity could be a useful tool to provide income security and certainty," MacSymon says.

Hugo does not believe a life annuity is a viable solution for age gap couples. In the current low interest rate environment, the likely yields from life annuities do not match what you can earn from a living annuity with exposure to equity markets. Life annuity companies base their guaranteed rates on the Consumer Price Index CPI and many income planning scenarios assume a thumb suck average inflation rate of six percent a year. But, she says, a retired couple's personal inflation rate may be much higher bearing in mind they can expect medical scheme costs to increase at about 10 percent a year. Second, annuity rates are based on age and gender: the younger you are at retirement, the lower the rate and rates for women are lower than those for men rates are based on age and gender: the younger you are at retirement, the lower the rate and rates for women are lower than those for men. Thus, in the typical age gap scenario of older husband and younger wife, the annuity rate will be even lower if they buy a joint and survivorship annuity. Hugo says that, apart from the better yield, the advantages of living annuities are investment flexibility recall the time weighted investment model and the fact that the capital reverts to the client on death. She says people approaching retirement can become too focused on their regular monthly income and overlook the crucial need for liquidity free cash to meet major, often unforeseen, expenses.

The bigger the age gap, the more important that funds are available to meet a number of these "balloon payments". Here again, the advantage of a living annuity is that a major expense can be met by increasing the drawdown rate to the maximum of 17.5 percent a year. Healthcare costs One of the major expenses faced by retirees is medical costs. It is sometimes assumed that the younger, healthier spouse will be able to serve as primary caregiver if the older spouse falls ill. However, this assumption underestimates the emotional and physical effort required to look after someone with an illness such as dementia. Therefore, age gap couples' budgets need to take account of the need for a caregiver or frail care, which, Hugo says, currently costs an average of R24 000 a month.

MacSymon says the timing of the decision to move into a retirement centre that offers frail care presents a dilemma for many retirees, particularly those with a substantial age gap, because many retirement centres have extensive waiting lists. "To be pre-mature or too late on the decision can create regret, and thus careful planning needs to be deliberated to accommodate both spouses' well-being." Second marriages Divorce, followed by a second marriage, is often a reason for a significant age difference between spouses at retirement. This can have unfortunate consequences for the younger spouse's retirement if the estate planning is not handled properly. People forget that retirement fund beneficiary nominations are not set in stone. Ultimately, it is retirement fund trustees who decide how to allocate benefits. Your former spouse's divorce order takes precedence over current spouse in claims against the estate. Also, financial settlements reached in terms of the divorce order may not be the end of the matter. Trustees can allocate benefits to a spouse who can prove financial dependency for example, by providing bank statements showing regular transfers for ad hoc expenses. Therefore, it is import ant that previously married spouses fully disclose their financial commitments to their ex-spouses and children so that the planner can take these liabilities into account when drawing up a retirement plan.

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