AGE-BASED INVESTING

Don't make these dumb moves with your nest egg

Sarah O'Brien, special to CNBC.com
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By now, we all know we should be saving for our golden years. But financial advisors caution that retirement planning goes far beyond simply building a nest egg.

While the mistakes that people can make are myriad — after all, who's a pro about the many aspects of retirement planning except the pros? — here are some of the situations that seem to often crop up.

1. Inappropriate investments. Sometimes advisors review a potential client's financial picture and are dismayed to discover that although decades were spent saving for retirement, the money was languishing in cash or bonds instead of invested in the stock market. That means the person's retirement portfolio could be worth about a third of what it could have been if it had been

invested more aggressively.

Other times, people take too much risk in the market at a time when they absolutely should not.

Advisor Jennifer Landon had a client who, before he came to her, cashed out of his pension plan when he retired in his mid-50s. He put the money in an individual retirement account and went whole hog in the stock market.

However, because he no longer had a source of income, he took advantage of Internal Revenue Service Rule 72(t).

Rule 72(t) allows you to take advantage of your retirement savings before the age of 59½, when there is otherwise a 10 percent penalty on early withdrawal. The withdrawals, however, are still taxed at your income rate. The drawback to taking advantage of Rule 72(t) is that you may deplete your retirement accounts well before the end of your life expectancy. By taking out your funds early, you are putting yourself in jeopardy in the future.

Once a 72(t) plan is implemented, you are locked into it.

The problem was that he did all this right before the market imploded. And because he was required to take the 72t payments — which totaled roughly $50,000 a year — he was forced to liquidate stock holdings when the market was low.

"You can't have money you need in the short-term invested in a lot of risk," said Landon, owner of Journey Financial Services.

Advisors also see people invested too heavily in one asset. Craig Ferrantino, founder and principal of Craig James Financial Services, had a client who received nearly $900,000 as a lump sum from his pension plan. Despite Ferrantino's advice, the client invested most of it in a real estate property in Florida. Its value has been cut in half.

"Don't sacrifice your retirement for the sake of a fly-by-night exciting thing, because it might not work out," he said. "You should also always be diversified."

"Even if you have a good plan going into retirement, be proactive about the … potential things that can blow it up."
-Mark LaSpisa, president and managing advisor at Vermillion Financial Advisors

2. Failure to update. Ferrantino also had a married couple as clients who, after their marriage failed, each separately retained his services. The wife was a penny-pincher and the husband a spendthrift.

After the divorce, the wife changed her will to make sure that only her children would be entitled to her estate.

Ferrantino reminded her several times that she needed to update the beneficiary form for her

retirement portfolio — which was worth seven figures — to ensure that it reflected what was in her will. But the client, who was in her 50s and still working, probably thought she had plenty of time to make the change.

Unexpectedly, she suffered a heart attack and passed away, which meant her ex-husband remained the beneficiary of her retirement funds.

"She went through the process of changing her will but not changing beneficiaries, so the ex-husband was entitled to all her retirement money," Ferrantino said.

While it might seem odd that a simple beneficiary form for a retirement account supersedes intentions stated in a will, the fact is that it typically does.

In simple terms, retirement accounts such as IRAs or 401(k) plans are not considered part of the estate covered by a will. The same goes for other financial accounts, such as insurance policies and annuities.

And while a person named in the will can challenge an account beneficiary, doing so can be a drawn-out, pricey legal process that might still result in the listed beneficiary receiving the money.

So what is the lesson? "Make sure you keep all your records updated, particularly when you have a material change in your [life]," Ferrantino said.

3. Giving away too freely. The mother of a client of certified financial planner Mark LaSpisa had a charitable heart. While that was an admirable quality, the mom, in her early 60s, was susceptible to giving away so much of her money that she was in danger of compromising her own retirement.

The final straw for the son — LaSpisa's client — was when the mother's favorite local charity called to ask if she could replace its broken-down bus and she wrote the organization a check for $80,000. And that's when her son put his foot down.

That $80,000 represented about 20 percent of her estate. In other words, she could not afford that kind of donation.

The son came in and said, 'No more. She is not to make these donations,'" said LaSpisa, president and managing advisor at Vermillion Financial Advisors.

"He wanted to make sure someone was watching the cookie jar so it wouldn't happen again," he said.

The mom began meeting monthly with LaSpisa to have her checkbook balanced and her expenditures monitored.
LaSpisa explained that living beyond her means is one thing that can derail her retirement.

"This can be spending too much or giving away too much," he said.

4. Failure to strategize. DC Chamberlin, a CFP with the Chamberlin Group, said his firm often sees mistakes involving Social Security payments.

Eligibility for Social Security benefits starts at age 62, but full retirement age — as viewed by the government — ranges from age 65 to 67, depending on when you were born. If you start taking benefits before your full retirement age, your monthly check will be reduced.

Say your full retirement age is 66 and you're due $1,000 monthly. If you start taking Social Security at age 62, your payment will be $750, a 25 percent reduction.

But if you wait until age 70, your monthly benefit will be $1,320 vs. $1,000.

"If you start taking it at age 62 vs. 70, you're losing out on [a lot] of your potential benefit, and that can cost you down the road," Chamberlin said. "If you can, delay taking it until age 70."

Other mistakes that advisors see run the gamut from being taken advantage of by predators (whether for financial products or other things, like late-night TV product sales) to not maximizing favorable taxes and having inadequate insurance.

"Even if you have a good plan going into retirement, be proactive about the … potential things that can blow it up," LaSpisa said.

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