

Making Everything Easier!™

2nd Edition

Personal Finance After 50

FOR
DUMMIES®
A Wiley Brand

Learn to:

- Understand how changes in government programs can impact your retirement
- Consider the implications of tax laws
- Navigate your saving and investment options

Eric Tyson
Bob Carlson

*Coauthors of the first edition of Personal Finance
After 50 For Dummies*



Introduction

We're all getting older, together. Aging presents opportunities for increased wisdom and broader perspective as well as some increased challenges. One of those challenges has to do with finances. The new, and sometimes more complex, financial decisions that confront folks in their later working years and then in retirement can be tough to work through.

For example, consider the types of questions we, your humble authors, have been asked from folks in our advisory businesses:

- ✓ Can we afford to retire? How much can we comfortably spend per year given our assets?
- ✓ My employer is offering me pension options. How do I choose among them?
- ✓ I just left my employer (by choice or through layoff) and have some money in a retirement account. What should I do with it?
- ✓ How should I manage my investments now and in the years ahead? When should I begin collecting Social Security benefits?
- ✓ What's the process for withdrawing money from my retirement accounts, and how can I minimize my tax hit from doing this?
- ✓ Should I buy an annuity? If so, what type? Are reverse mortgages a good idea?
- ✓ What types of additional medical insurance — long-term care insurance, Medicare supplement, and so on — do I need pre- and post-retirement?

- ✓ An agent is telling me to buy more and different life insurance. How much do I need and what type of life insurance should I buy?
- ✓ Do I need a will? Do I need an estate plan? What should I do to protect my spouse, children, or significant others?

We wrote this book to answer these questions and many more that face you as you age and grapple with your finances during your senior years. We hope to not only answer your questions but to also make you aware of important issues you may not be aware of so you have plenty of time to consider them and make decisions that enhance your financial independence.

About This Book

Everyone needs to make financial decisions. Whether you're rich, middle class, or poor, 50 or 85 years old, retired, or still working two jobs, money passes through your hands every day. No matter your situation, we're excellently positioned to give you sound financial advice on the range of issues presented in this book. We each have decades of professional experience in the financial services industry; we each have extensive training and background to provide expert personal financial and retirement advice; and we both communicate in plain English with our readers, operate free of conflicts of interest, and interact with people like you with real financial problems that need solutions.

Eric started as a management consultant in the financial services industry and then worked as a personal financial counselor. Now he's an author and the proprietor of www.erictyson.com. Eric is a trained economist who graduated with honors in Economics from Yale

University. Bob is Chairman of the Board of Trustees of the Fairfax County Employees' Retirement System, which has more than \$3 billion in assets. He has served on the board since 1992. He's also the editor of the monthly newsletter, *Retirement Watch*. Bob received his JD and an MS in Accounting from the University of Virginia and received his BS in Financial Management from Clemson University and passed the CPA Exam.

We also have established a few conventions to help you navigate through this book: First, although we'd like to believe that you want to pore over every last word between the two yellow and black covers, we make it easy for you to identify "skippable" material—information that's interesting but not essential: text in sidebars (the shaded boxes that appear here and there) and paragraphs marked with a Technical Stuff icon. Second, we put all web addresses in monofont for easy identification. If a web address breaks across two lines of text, just type it in exactly what you see it in this book, pretending as though the line break doesn't exist. (If you're reading this book online, simply click the link to go to the webpage.) Finally, we refer to the decade from 2000 to 2009 as the *2000s*. We just wanted to avoid any confusion in case you were thinking of the year 2095.

Foolish Assumptions

When writing this book, we made some assumptions about you:

- ✓ You're age 50 or older (or rapidly approaching that age) and are approaching or are in retirement.
- ✓ You're still in the workforce and have no plans to retire, which is fine and compatible with our approach in this book too.

- ✓ You want expert advice about important financial topics, and you want easy-to-understand answers.
- ✓ You want a crash course in personal finance and are looking for a book you can read to help solidify major financial concepts and get you thinking about your finances in a more comprehensive way.

Throughout this book, we offer many resources, including websites and online tools to help you, as well as plenty of alternative off-line resources and assistance.

Icons Used in This Book

The icons in this book help you find particular kinds of information that may be of use to you. Here's a rundown of what each icon means:



This target flags strategy recommendations for making the most of your money.



When you see this icon, you'll know the text next to it points out information that you definitely want to remember.



This icon marks things to avoid and points out common mistakes people make when managing their finances.



This icon alerts you to scams and scoundrels who prey on the unsuspecting.



The investigate icon tells you when you should consider doing some additional research. Don't worry — we explain what to consider and what to look out for.



This icon appears beside discussions you can safely ignore because they aren't critical to your understanding of the topic at hand; however, reading them can help deepen your personal financial knowledge.

Beyond the Book

In addition to the material in the print or e-book you're reading right now, this product also comes with some access-anywhere goodies on the web. Check out the free Cheat Sheet at

www.dummies.com/cheatsheet/personalfinanceafter50 for information about employer pensions and go to www.dummies.com/extras/personalfinanceafter50 for articles that explain the evolution of long-term care, offer advice on how to answer Medicare questions, and more.

Where to Go from Here

This book is organized so you can go wherever you want to find complete information. Want advice on managing and tracking your expenses in retirement? See [Chapter 6](#). If you're interested in investing strategies and developing a retirement plan, cruise on over to [Part II](#). If you're not sure where you want to go, you may want to start with [Part I](#). It gives you all the basic info you need

to assess your financial situation and points to places where you can find more detailed information for improving it. Check out the table of contents for a chapter-by-chapter rundown of what this book offers. You also can look up a specific topic in the index. Last but not least, you can turn to [Chapter 1](#) and begin reading for a complete and thorough crash course in personal finance during your golden years.

Part I
**Working toward
Retirement**

getting started
with

**Finances
After 50**



Visit www.dummies.com for great (and free!) Dummies content online.

In this part ...

- ✓ Get complete and easy-to-understand guidance on how to best plan for a secure financial future
- ✓ Learn how to protect your employment income.
- ✓ Develop a plan that will see you through your retirement years by discovering the best retirement investments and strategies, and understanding retirement account rules

Chapter 1

Looking Ahead to Your Future

In This Chapter

- ▶ Taking charge of your long-term plans
 - ▶ Implementing retirement planning strategies
-

From a young age, various adults in our lives tell us to plan ahead. Although it may be sunny and clear outside this morning, they tell us to take rain gear for this afternoon's possible heavy rain. When packing for a day at the beach, they suggest sunscreen and money for lunch. And do your best in high school, they say, because your transcript will in part determine which colleges accept you.

Although some parents provide guidance to their children on the topic of long-term financial planning, most don't because they aren't sufficiently knowledgeable or are reluctant to explain these things to their kids. And therein lays a pretty significant problem concerning finances for your adult and especially later adult years.

And retirement has its own set of trials. Unexpected life events (such as a loss of a job, the death of a loved one, or a major medical problem) and economic challenges can throw a wrench in the best plans. The severe recession and stock market decline in the late 2000s — both of which were the worst in decades — highlighted other potential planning obstacles. Many near retirees

and recent retirees caught off guard face the possible need to keep on working beyond typical retirement age, the need to reduce spending and make do with less (for example, one car rather than two), and the need to cope with diminished investment portfolios and declining home values.

These challenges can occur at any time during life, but they're especially challenging when they happen when you're in or near retirement. You have less time to make up for setbacks (and any mistakes you make) as you age. At some point in most folks' lives, working longer or going back to work no longer are viable options. That's why planning and regularly reviewing and re-evaluating your plans is essential.

We know many of you are reading this book having done little or no planning to this point. Don't worry, though. It's never too late to start planning. Studies of retirees show those who are most content in retirement are those who did some planning, even if it was a small amount. Planning is how you match your resources with your goals and expectations and identify where adjustments need to be made. Even if you're already retired, planning now can improve the rest of your retirement.

This chapter discusses important themes that run throughout the book: the value of planning ahead and getting on the best path as soon as possible, the importance of taking personal responsibility, and the significance of taking a long-term perspective to make the most of your senior years. We also discuss how to keep the right focus to optimize your retirement planning.

Planning for the Longer Term

Planning doesn't sound fun, and for many people, it isn't one of life's most enjoyable activities. But nearly everyone values the benefits of proper planning: peace of mind, financial security, more options and choices, improved health, and a better lifestyle.

During your senior years you have many choices about different financial issues. You can change some of the decisions after you make them, but others can't be altered. If you do decide to make adjustments, you have fewer years to benefit from the new choices. That's why as you approach your senior years, planning your finances is more important than it was earlier in life.

In this section, we discuss the important issues that warrant your planning attention, explain why you should be the person to take the most responsibility for making that happen (even if you hire some help), and quantify the value of your taking our advice.

Identifying long-term planning issues

What's on your mind (or should be on your mind) regarding your financial future? Consider how many of the issues in the following sections require long-term planning.

Choosing among an employer's pension options

You need to look not just years but decades into the future to determine which pension option may best meet your needs and those of your loved ones. A *pension* is an

employer-provided retirement benefit from money that your employer puts away on your behalf, wherein you receive a monthly payment based on your years of service and earnings. A pension typically is just one of several sources of retirement income you may have (the others typically being Social Security and personal savings including retirement accounts), so you must consider how these will fit together over many years.

Pensions (check out [Chapter 7](#) for more info) differ from other sources of income, such as 401(k)s, IRAs, profit-sharing plans, and employee stock ownership plans (ESOPs), mainly in that only pensions guarantee you a fixed payment backed by your employer. With other types of retirement savings, the amount you receive in retirement depends on the amount you contribute and how you invest the account. See [Chapter 5](#) for more info on other retirement accounts.

Leaving an employer and deciding what to do with your retirement account money

When you change jobs, get laid off, or retire, you often are faced with choices about when and how to withdraw money from retirement accounts — such as 401(k)s or 403(b)s — and minimizing the tax hit from doing so. Moving money is a decision you have to make today, but don't make light of this decision because the decision affects how much money you'll have in the decades to come.



Some employer plans allow you to keep retirement money in place even if you're no longer employed with the company. You may choose to accept the offer to keep money in place if it's a plan with good investment options and low costs. Planning

retirement account withdrawals requires long-term tax planning if you want to make the withdrawals in the best way possible. For more information on handling retirement accounts, see [Chapter 5](#).

Determining whether you can afford to retire and how much you can safely spend per year

To assess whether you can afford to retire and how much you'll be able to spend after you do retire, you have to do some analysis relating to your spending habits and investing holdings and temperament. And, to be sure that you don't run out of money or come close to running out of money, you also need to consider a wide range of scenarios for how your investments may perform in the years ahead. You can't assume investments will return their historic averages each year. In fact, we've seen some stock indexes generate low returns or even negative returns over periods of a decade or more. See [Part II](#) for more information on each of these issues.



As with other aspects in life, differentiate between the things you can control and the things that you can't. The economy will go through recessions and the stock market will decline. Predicting their timing, depth, and duration is beyond anyone's control. Although you can't control these events, you can be prepared for them. Your plan should reflect that by having some flexibility and, if possible, a cushion. For example, you can control some of your spending and how much risk you take investing.

Deciding when to begin collecting Social Security

Deciding when to begin collecting your Social Security is a complicated decision that's impacted by many factors,

including tax laws, your earnings and your spouse's earnings, marital status, and your health, among others. As we discuss in [Chapter 10](#), you have to look years and decades ahead to make an appropriate and successful decision.

Considering a reverse mortgage

Reverse mortgages are becoming increasingly popular to provide supplemental retirement income to cash-poor (and relatively house-rich) elderly. With a *reverse mortgage*, you receive payments (or a lump sum) from the lender. Interest on the loan (and fees) compounds, but the debt doesn't have to be paid until the home is sold. When you consider taking out this type of mortgage, you should do plenty of long-term analysis to compare your options and be sure you're getting the right one for your situation. See [Chapter 8](#) for the details.

Contemplating additional medical insurance

Health insurance is always a prickly issue to deal with because it's difficult to know what medical issues you may be facing 5, 10, 20, or more years from now. Sure, you can gain a general sense from your parents and from the types of medical issues that aging adults confront, but only time will tell what unique issues you'll confront. Different options you have to consider pre- and post-retirement are long-term care insurance (see [Chapter 9](#) for more info) and Medicare supplements (refer to [Chapter 11](#)).

Weighing the option to buy more or different life insurance

When others are dependent on your employment income, you may need some life insurance coverage. And, depending on your specific assets, the type of life

insurance you may most benefit from may change over the years.



To determine your life insurance needs, you should have a good sense of your current financial assets and current and future obligations. Refer to [Chapter 2](#) for more information on evaluating your need for life insurance.

Developing your estate plan

Your financial circumstances of course will change in the years ahead, and so too will tax and probate laws.

Planning your estate involves many issues, including ensuring your own financial security, taking care of your affairs in the event you're unable to do so yourself, and protecting and providing for your heirs. Head to [Part IV](#) to find out more.



Be aware of and involved in your investments

Keeping a close eye on your investments and knowing what's going on with your money is important, particularly during your senior years. You should never blindly trust someone with your money.

Consider the victims who lost tens of billions of dollars to hedge fund Ponzi-schemer Bernard Madoff, many of whom were near or in retirement. The prime targets of the Madoff scam (and of most financial scams) were people in their 50s and older who worry about their standard of living and income, though they're what most people consider financially comfortable. Within this group was another target group: Entrepreneurs and successful professionals. Risk-taking usually is part of their personal profiles, and risk-takers often are attracted to unique and little-known strategies. That's why con artists seek them.

Madoff investors lost so much money in such a total fraud primarily because of a lack of homework. Victims failed to conduct proper research (or even any research) on Madoff's claimed returns. They simply invested with Madoff

due to the recommendations of others investing with him. With a private money manager like Madoff, investors should have been far better educated regarding his investing options and conducted lots of due diligence. They should have insisted on knowing what his investment strategy was and how it was supposed to work. They should have reviewed audited statements of the amount of assets he claimed to be managing. If they had, they would have noticed that the market for the stock options he claimed to be trading wasn't big enough to support his portfolio, much less all the other investors' trading options.

Interestingly, it has come out that Madoff largely refused to provide much information to inquisitive prospective investors and essentially blew them off and turned them away. In retrospect, such behavior makes sense because Madoff wasn't interested and didn't need to accept money from investors who were asking too many questions. After all, they may have uncovered his enormous fraud.

Taking personal responsibility for your financial future

Our lives are filled with responsibilities — jobs, family obligations, bills, household maintenance, you name it. We all try to make time for friends, fun, and recreation as well.

With all these competing demands, it's no wonder that many folks find that planning for their financial future continually gets pushed to the back burner. Most people don't have the time, desire, or expertise to make good financial decisions. But you've taken a huge step to erase those obstacles in buying this book. We provide sound counsel and advice, and now you're investing the time and energy to get on a better path toward retirement.



From this point forward, we urge you to always remember that you — and only you — can take full responsibility for your financial future. Of course, you can hire advisors or delegate certain issues to a willing and competent spouse or other beloved relative. But, at the end of the day, it's your money on the line, and you had better take an interest in it! Delegating your responsibilities without knowledge, understanding, and some involvement is a recipe for disaster. You could end up without vital insurance, be taken advantage of in terms of fees, or even defrauded among other unsavory outcomes.

Saving and planning sooner and smarter pays off

Throughout this book, we discuss financial strategies and tactics for making the most of your money over the coming decades of your life. The sooner you get control over and optimize your finances, the bigger your payoff will be.



You should never rush into making changes that you don't understand and haven't had time to properly research. Procrastination comes with many costs, including lost financial opportunities. Creating a financial plan and sticking to it is so important when planning for retirement. [Chapter 3](#) helps you make your own plan.

Consider, for example, something that nearly everyone wants to do: save and invest for future financial goals such as retirement. Take the case of the Fuller family, who came to Eric for financial counseling years ago. The

Fullers enjoyed a healthy and relatively stable income yet they saved little, if any, money annually. They knew how to spend money!

In terms of savings, they had about \$100,000, which sounds like a lot but given their annual income (\$150,000) and ages (late-40s), they still hadn't accumulated savings equal to a year's worth of income. The money they had wasn't well invested — nearly all of it was in low-interest bank accounts and a pricey life insurance policy that provided just \$500,000 of coverage (not near enough given their incomes and the fact that they had dependent children). Of course, they could have done worse (at least the money was growing slowly). However, they weren't going to reach their retirement goals unless their money started working harder for them.

Over a number of months, the Fullers worked with Eric and were able to implement the following changes, which they stuck with for the years that followed:

✓ **They increased their savings rate.** They were able to consistently save about 15 percent of their annual incomes (about \$22,500 per year), which was up from just 4 percent (\$6,000). They accomplished this through a combination of reduced spending and reduced taxes by directing their savings into tax-advantaged retirement accounts including a 401(k) and SEP-IRA.

“Cutting our expenses was easier than I thought. We were wasting money on things we didn't really need or even use in some cases,” said Mrs. Fuller. Her husband added, “We felt much more relaxed and less stressed by cutting our expenses and boosting our savings.”

- ✓ **They improved their investment returns.** Rather than earning a meager return having their money in low-interest bank accounts, the Fullers enjoyed 8 percent annual returns by investing in a diverse mix of stocks around the world along with some high-quality bonds.
- ✓ **They purchased better insurance coverage.** The Fullers needed about \$1.5 million of life insurance coverage — triple the amount they had been carrying. They were able to buy that increased level of coverage along with some additional needed disability insurance by raising their deductibles on some other insurance policies and by switching to lower-cost (but still high-quality) providers.

So what were these changes worth to the Fullers? As they themselves said, they had much more peace of mind and comfort with their new financial situation. In the remaining part of this section, we briefly examine the true financial value to them over the decades following the changes.

If the Fullers had continued saving as they had been (saving just 4 percent of their incomes yearly and keeping that money in a bank account), in 10 years (when they reached their late-50s), they would have accumulated \$188,000. This would have put them in a relatively poor situation for their future retirements given their annual income of \$150,000.

On the other hand, the changes (saving 15 percent annually and instead earning an average investment return of 8 percent yearly) would lead the Fullers to have more than \$541,000 in 10 years — nearly triple what they would have had if they hadn't made changes. The differences are even more dramatic looking 20 years out. Check out [Table 1-1](#) to see the calculations.

Table 1-1 The Long-Term Value of Saving and Earning More

<i>Number of Years</i>	<i>Status Quo (Save 4% per year, earn 2% per year)</i>	<i>With Changes (Save 15% per year, earn 8% per year)</i>
10	\$188,000	\$541,000
20	\$295,000	\$1,494,000

By making sensible changes, the Fullers are well positioned to retire with a hefty nest egg. (In fact, they could consider retirement sooner.) In the absence of those changes, however, they would have a small amount and be unable to even come close to maintaining their lifestyle during retirement.

Eyeing Keys to Successful Retirement Planning

Although you may like to consider other factors — such as your health, relationships with friends and family, and interests and activities — as more important than money, the bottom line is that money and personal financial health are extra-important factors to your retirement lifestyle.



Getting caught up in planning the financial part of your future is easy. After all, money is measurable and so much revolves around the money component of retirement planning. So what can you do to successfully plan for retirement? You could simply work really hard and spend lots of time making as much money as possible. But what would be the point if you have little free time to enjoy yourself and others? Fortunately you can implement the following strategies when planning for retirement. We weave discussions on these important issues throughout the book.

Saving drives wealth

You may think a high income is key to having a prosperous retirement, but research shows that the best way to retirement bliss is to save. Research demonstrates that wealth accumulation is driven more by the choice to save (rather than spend) than it is by a person's income.

For example, professors Steven Venti and David Wise examined nearly 4,000 households across an array of income levels that challenges the notion that many households lacking high incomes don't earn enough money to both pay their bills and save at the same time.

Venti and Wise examined these households' current financial statuses and histories to explain the differences in their accumulations of assets. Their findings showed that the bulk of the differences among households, " ... must be attributed to differences in the amount that households choose to save. The differences in saving choices among households with similar lifetime earnings

lead to vastly different levels of asset accumulation by the time retirement age approaches.”



It’s not what you make but what you keep (save) that’s important to building wealth. Of course, earning more should make it easier to save, but most folks allow their spending to increase with their incomes.

Keeping your balance

Most people we know have more than one goal when it comes to their money and personal situations. For example, suppose Ray, age 50, wants to scale back work to a part-time basis and spend more time traveling. He reasons, “I don’t want to wait until my 60s or 70s, because what if my health isn’t great or I don’t make it!” But Ray also wants to help his adult children with some of the costs of graduate school and possibly with buying their first homes.

Ray’s situation — of having multiple goals competing for limited dollars — is often the norm. Thus, a theme we discuss throughout this book is how to trade off competing goals, which requires personal considerations and balance in one’s life.



Unless you have really deep pockets and modest goals, you need to prioritize and value each of your goals.

Understanding that planning is a process

The Aircraft Owners and Pilots Association has a slogan: “A good pilot is always learning.” Likewise, to have a

good retirement you almost always need to be planning. Financial planning is a process. Too many people develop financial plans and then think they're finished. Taking this route is a good way to run into unpleasant surprises in the future.

A plan is based on assumptions and forecasts. However, no plan — no matter how carefully it's developed — gets all the assumptions and forecasts correct. Even your best, most careful guesses may miss the mark. So every few years, you need to review your plan.

As you're reviewing, assess how much reality differed from your assumptions. Sometimes, you'll be pleasantly surprised. Your portfolio may earn more than you expected, or you may spend less than you estimated.

Other times the review won't be as pleasant. The markets may have dragged down your portfolio returns. Or your spending may have exceeded your estimates. In either case, you aren't reaching your goals.

Even if you do meet the mark in most instances, you still are never really done planning and revising. You're bound to experience changes in your life, the economy, the markets, tax law, and other areas. You may come across new opportunities that weren't available a few years ago or that weren't right for you then but make sense now. You need to continually adapt your plan to these changes. You may need to adjust your spending or change your investment portfolio.



You don't have to be obsessive. Daily, or even quarterly, changes in your portfolio that are different from the plan aren't a reason to go back to the drawing board. But every year or two (or when you have a major change in your personal situation) take a fresh look. Review the plan and your progress. Figure out what went right and what went wrong. Decide whether your goals or situation have changed and whether any adjustments are needed. Finally, implement the new plan and enjoy life. After all, that's what the money is for.

Chapter 2

Protecting Your Employment Income and Your Health

In This Chapter

- ▶ Evaluating your need for life insurance
 - ▶ Seeing why most working people need disability coverage
 - ▶ Making the most of your health
-

During your working years, especially your earlier working years, your future income earning ability is probably your most valuable asset. Consider that the typical person in his 20s and 30s has many years (decades, in fact) ahead of him to earn money to feed and clothe himself and make other expenditures (for example, transportation, taxes, medical bills, and vacations) and save for the future. Unless you're independently wealthy (or have a deep-pocketed relative ready to provide long-term care for you if you hit hard times), you should carry the proper types and amounts of insurance to protect yourself and your family if something occurs to you that would affect your ability to earn a living. In this chapter, our focus is on protecting income you're earning while employed.

Insurance isn't free, of course. And, like other companies, insurance companies are in business to turn a profit. So you want to make sure you obtain proper

insurance protection at a competitive price and buy only the coverage you need.

In this chapter, we dive into the details regarding life and disability insurance you may need. Here we also discuss your employment income and how best to protect it. Finally we also cover the importance of making the most of your health to minimize the chances of future insurance claims. If your health isn't good as you enter retirement, you're going to have more issues to face than just those dealing with your personal finances. So getting your health in order is important.

Assessing Your Need for Life Insurance

Needing insurance is kind of like needing a parachute: If you don't have it the first time you need it, chances are you won't need it again. Regarding your need for life insurance, of course, you don't get second chances. (Unless you're considering near-death experiences; and the life insurer doesn't pay out for those!) So if you "need" life insurance, you should get it as soon as possible.

The following sections explain what life insurance can do for you. They also help you determine whether you need insurance, and if you do, how much you should consider buying.

Understanding the purpose of life insurance

The primary reason to consider buying life insurance is to provide financially for those who are dependent on your employment income. However, just because you

have a job, earn employment income, and have dependents (children, a spouse, and so on) doesn't mean that you need life insurance.

So how do you know whether you need life insurance coverage? Your current financial situation is an important factor in determining your need. If you haven't already assessed your retirement plan and tallied your assets and liabilities, be sure to read [Chapter 3](#).



If you're still working, aren't financially independent, and need your current and future employment income to keep up your current lifestyle — and you're saving toward your financial goals — life insurance probably is a good choice. If you have others depending on your employment income, you generally should get term life insurance coverage (which we discuss in the later section "[Figuring out what type to buy](#)").

On the other hand, you may find that even though you're still working, you've achieved financial independence. In other words, you've accumulated enough assets to be able to actually retire and no longer need to earn employment income.

For example, consider one extreme: Microsoft founder Bill Gates has dependents and he doesn't need life insurance to protect his current income. That's because he has billions in investments and other assets to provide for his dependents. Of course, the rest of us aren't Bill Gates! But we bring up this enormously successful entrepreneur in this discussion to drive home the crucial point that if you've accumulated significant enough assets compared to your annual living expenses, you may not need life insurance.

Determining your life insurance need

Each person's circumstances vary tremendously, so in this section we don't tell you specifically how much life insurance to get. Instead, we show you the factors you need to look at in order to determine that amount. We're not fans of general rules like getting ten times your annual income in coverage, especially for those approaching or already in their senior years. The reason? Each person's circumstances can vary tremendously among many factors such as

- ✓ **Your assets:** Generally speaking, the more you have relative to your income and obligations, the less life insurance you need.
- ✓ **Your debts:** Of course, not all debts are created equal. Debts on real estate or small businesses tend to have lower interest rates, and the interest is often tax-deductible. But the more of this type of debt you have, the more life insurance you may need. On the other hand, consumer debt — such as credit card and auto loan debt — tends to be at higher interest rates, and the interest generally isn't tax-deductible. But again, the more of this debt you have, the more life insurance you're likely to need.
- ✓ **Your health and the health of your family members:** If you have major medical problems or have a family member who's ill or who has special needs, you may need more coverage.
- ✓ **The number of children you need to put through college:** A four-year college education, especially at private schools, is a major expense. So, if you have kids to put through school — and they may attend costly schools — you could be talking some really big

bucks. And you face even bigger bucks if you want to help them through graduate or professional school after college.

- ✓ **Whether you'll have elderly parents to assist:** Of course, this factor is difficult to predict, but you should have some sense of your parent's physical and financial health. If you don't, try to broach the topic in a sensitive fashion with them.



After completing your retirement planning (see [Chapter 3](#)), you should have the current financial information you need to begin your calculations for how much life insurance you need. Here's a quick and simple way to determine how much life insurance to consider buying:

- 1. Determine your annual after-tax income (from working, not investments).**

You can find this number on your tax return or W-2 form from the past year. (The reason you work with after-tax income is because life insurance death benefit payouts aren't taxed.)

- 2. Determine the amount of money you need in order to replace your income for the appropriate number of years.**

You can find this amount by simply using the information in [Table 2-1](#).

- 3. Consider your overall financial situation and whether you need to replace all your income over the time period you chose in Step 2.**

High income earners who live well beneath their means may not want or need to replace all their