

REAL SIMPLE

EVERYTHING YOU NEED TO KNOW ABOUT PHASED RETIREMENT

Phased retirement is a concept that's gaining momentum—and popularity.



By: Erik Sherman - April 22, 2021

If you haven't yet heard the term "phased retirement," don't worry; you're not alone. It's still a relatively under-the-radar concept in the retirement world, one that still has a long way to go to become widely understood or adopted.

According to the professional journal SHRM (Society for Human Resource Management), among U.S. workers age 61 to 66, a mere 29 percent say they plan to take some sort of phased approach to retirement. Meanwhile, the share of organizations offering select employees a phased retirement approach (on an informal basis) has risen in recent years, reaching 15 percent among employers that responded to a 2019 SHRM benefits survey. The roll-out of more formal phased retirement programs, which are broadly available to all employees, has stalled at around 6 percent.

So, what is phased retirement exactly? And is it something you should be contemplating as well? Or at the very least asking your employer about?

As SHRM explains, phased retirement allows older employees to reduce work hours gradually, creating a kind of slow transition into retirement rather than a sudden departure from the workforce. In addition to reducing work hours over time, these programs include initiating a partial drawdown of retirement funds from defined contribution or defined benefit retirement plans, says SHRM. Also worth noting, this approach to slowly disengaging from work also include continued employer-sponsored health coverage until you fully leave the workforce.

If all of this sounds intriguing, here are a few more insider tips about phased retirement and its potential pros and cons.

Practice makes perfect

Let's start with the obvious. Retirement is one of the biggest life transitions we will ever make. And whether we're talking about playing a sport, running a business, or basic life skills, humans perform better and achieve more successful outcomes when they've had the opportunity to practice a skill.

"Phased retirement allows the retirement experience to be practiced," says Eric Ross, a certified financial planner and senior wealth advisor with Cincinnati, Ohio-based Madison Wealth Management. "During this practice period, one can begin doing the things they think they may like to do in retirement. If practice goes well, then you have a green light to move to full retirement or possibly continue in the phased approach if that's working for you."

This type of practice phase allows you to find the things that work well for you and the things that may not, adds Ross. The key is that it's important to be intentional about your practice.

"This can be accomplished by identifying ways in which you plan to spend your time during retirement. For example, you may anticipate spending more time with your children and grandchildren. You may discover this works well or you may also discover that can be too much of a good thing," says Ross. "Or your idea of spending more time together does not match what your children consider to be an ideal amount of time to spend together."

Phased retirement can help minimize use of retirement funds

Depending on how long you stretch out your phased retirement, this approach can help take some of the stress off your nest egg, allowing for a gradual reduction in earned income (as opposed to immediate departure).

"Once the income generated from a professional position stops, there's a natural tendency to apply more attention and pressure to a retiree's other sources of income that will support them in retirement, such as pension or investment portfolio," says Brian Niksa, senior wealth advisor for Capstone Financial Advisors. "A gradual reduction in earned income allows the retiree to minimize the pressure they would otherwise put on their portfolio or other outside retirement income sources."

Mental health

Having a continued outside source of earned income can help reduce some of the mental anxiety or stress associated with making such a monumental life change.

Many people tie a lot of their self-worth and identity to their careers and productivity. If you've had a career for decades, it can be difficult to differentiate your work self from your home self, and retirement can be a jarring change," adds Jeffrey Zhou, CEO of Fig Loans. "Losing that identity can trigger depression, anxiety, and a sense of loss in retirees. Phasing retirement can help you adjust to schedules that are less and less rigorous, and workloads that diminish over a period of time. This way you can acclimatize to the retirement lifestyle rather than jump in headfirst."

Succession planning

Though this may be of less concern to you as the employee, phased retirement can also be incredibly helpful for your employer. This approach allows for a thoughtful transition of knowledge.

"With traditional retirement, someone has to pick up where the retiree left off, with potentially months of catch-up to get back up to speed," says Zhou. "With phased retirement, future retirees can prepare someone for their position and employers can support that preparation with training and mentorship."

As SHRM notes, by the time an employee announces their fully ready to retire, it's often too late to begin such a knowledge transfer if it hasn't been underway already. Many forward-looking organizations get this, which is why they're often the leaders in the phased retirement space.

Potential reduction of Social Security benefits

While there are many obvious upsides to a phased approach to retirement, you'll want to be mindful of drawbacks as well. For instance, pursuing a phased retirement strategy has the poten-

tial to cause an unintentional reduction in your social security benefits, says Niksa, of Capstone Financial Advisors.

"Anyone who is eligible for Social Security has a defined full retirement age (FRA) based on their date of birth. If Social Security benefits are elected to begin before full retirement age, and income is still being generated, the benefits received from Social Security could be reduced," Niksa explains.

The reduction that applies to those who claim benefits prior to their full retirement age can be quite significant, adds Niksa, as much as \$1 for every \$2 earned over the Social Security earnings limit.

"In 2021, that limit is \$18,960," notes Niksa. "So anyone who is considering claiming their Social Security while still working and who has not yet reached their full retirement age should be mindful of this potential implication."

Not everyone's a fan

At least some financial advisors remain skeptical of this path of incremental retirement. Ryan Cicchelli, founder of Generations Insurance & Financial Services in Cadillac, Michigan, says phased retirement could very well exacerbate the existing crisis in America of people not being financially prepared for life after work.

"People have been underestimating their retirement needs for years. Phased retirement options likely include some form of early access to retirement benefits that may dwindle a retiree's overall pool of retirement benefits," says Cicchelli. "Coupled with the possibility of receiving a reduced regular income at an earlier date than planned, phased retirement could lead to the need to access retirement savings earlier than planned. This brand of semi-retirement will simply be insufficient to meet the needs of some prospective retirees in the long-term."

On the fence? Talk to a professional

Successfully planning for retirement can be tricky for the best of us, but especially for those who need to live within a carefully constructed retirement budget. Opting to take phased retirement can have a drastic impact on your overall retirement funds and game plan. Before jumping on board with this approach, it's best to crunch the numbers with a professional.

"Plan everything out with an advisor who can assess a phased retirement plan's options and help decide whether you're a good candidate for this type of program," suggests Cicchelli. "A financial professional can provide an estimated outlook on the potential financial impact and even make recommendations for alternative measures if necessary."

And remember, even when taking a phased retirement approach, there's a good chance you'll live a long life in full retirement, and you'll need your savings to last.

"Saving enough to make work optional or allowing for part-time work at potentially lower pay requires advance planning," says Rob Williams, vice president of retirement and financial planning for Charles Schwab, echoing Cicchelli. "Saving enough, accounting for healthcare costs, and thinking ahead about how you'll spend your time are all critical."

Ryan Cicchelli, founder of Generations Insurance & Financial Services, is committed to providing clients with financial security through a personalized, friendly approach. Ryan's top concern is helping clients make informed decisions about all things related to healthcare and retirement.

To contact Ryan, call 231-878-7074 or visit www.GenerationsIFS.com



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