CPA Practice Advisor

financial planning rules.

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We hear a lot about financial planning "rules of thumb," such as the 4-percent withdrawal rule, the 80 percent of pre-retirement income rule, the rule of 100 and many others.

It's important to have a track to run on when it comes to retirement planning, but you may want to exercise a bit of caution in putting too much weight on these financial-planning rules.

How well do they work? Do they work for all shapes and sizes of portfolios? How will you know if your personal situation matches up well with each financial-planning method? One of these rules may work better for you than for someone else, and vice

plans, it's advisable to include other types of investments in your plan such as annuities, REITS, etc.

• **The 4-percent withdrawal rule.** This rule is probably one of the most popular. The rule says that if you need to take regular or systematic withdrawals from a retirement portfolio, as long as you don't pull out more than 4 percent of your total portfolio value each year, you have a better chance of that income lasting throughout your retirement.

This rule assumes a 60/40 allocation of stocks and bonds – 60 percent stocks and 40 percent bonds. Similar to the Rule of 100, you may not want to put all of your eggs in one basket. There are many other choices in the investment universe and diversification is a vital component in any investment plan.

The "sequence of returns" risk is another factor to consider. If you are withdrawing 4 percent from your portfolio as this rule suggests, your annual income will change from year to year due to fluctuations in that portfolio value. Those fluctuations are entirely dependent on market conditions. Many would rather have a predictable and stable income in retirement.

• **The 75-to-80-percent rule.** This rule assumes you'll need 75 to 80 percent of your annual pre-retirement income to have a comfortable retirement. This is simply not the case for many people. Everyone's situation is different when it comes to retirement income needs. Some people like to travel all over the world, and some refuse leave the town where they live.

Some like to eat out, and some prefer home cooking. Some drive a luxury car and some an economy car. The amount you will need in retirement requires a solid retirement plan that factors in all of these items as well as taxes, inflation, medical needs, fixed and discretionary spending, and much more.

As you can now see, your path to a comfortable retirement should not be based solely

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