GLENMEDE
PRIVATE WEALTH

Retirement: A Balancing Act

Success in retirement requires more than a large nest egg; you also need a well-managed balancing act.

A lifetime spent accumulating wealth does not prepare us for the complexities of managing these assets in retirement. As holdings increase, inventive planning strategies become as important as an investment policy statement and asset allocation. Some of the many factors and variables to consider include inflation, personal cash flow needs, income taxes, long-term financial responsibilities, family legacy and charitable giving.

The transition to retirement should be navigated with a comprehensive yet flexible plan, one that works to:

- Minimize income and estate taxes through asset selection and location
- Balance long-term investment opportunities and current lifestyle needs
- Enhance personal legacy through strategic gifting and philanthropy

To this end, we find it helpful to divide retirement planning concerns into three categories:

- Current cash flow
- Lifetime asset base
- Family legacy and philanthropy

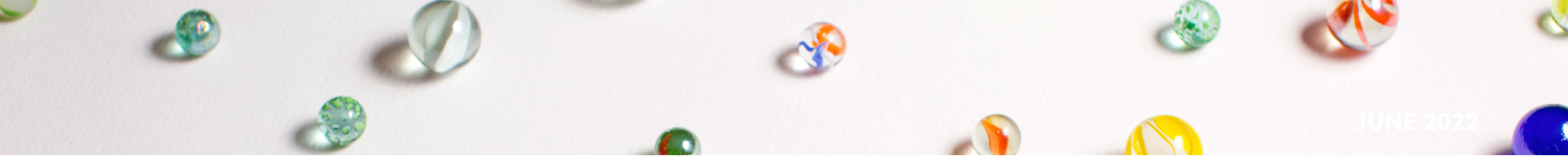
Each category has its own management challenges and risk considerations that will shift in importance over time. To help prepare for the transition to retirement, a detailed cash flow analysis will help set a balance between the need for current income generation and the long-term capital appreciation necessary to preserve a lifetime asset base. This tension between income and growth is especially delicate for the new wave of retirees who enter this phase of life without a defined benefit pension plan.

Current cash flow

In a low interest-rate environment, considerable capital may be necessary to generate annual cash flow great enough to fund current expenses. Investments in this category should be characterized as liquid and low risk. In addition, we recommend holding 6-12 months of cash in reserve to help avoid ill-timed asset dispositions.

To begin the process of evaluating near-term cash-flow needs, income streams such as pensions, deferred compensation and Social Security should be evaluated. Often the timing of these payments can be adjusted to allow for beneficial income tax planning and investment impact.

For example, an executive with deferred compensation payouts that begin upon retirement can delay pension and



Social Security payments in order to reduce current income taxes and maximize future fixed income streams. Healthy couples can maximize Social Security payments by suspending individual benefits until age 70 to allow for increased growth of future benefits. Conversely, for couples with little guaranteed income from pensions, an earlier Social Security payout may be desirable to keep the investment portfolio intact for as long as possible.

Retirees over the age of 72 should conduct special planning for required minimum distributions from qualified retirement accounts. Because these distributions are subject to ordinary income tax rates, these accounts can fund near-term cash flow needs, leaving a greater percentage of taxable investments for longer-term investing.

Lifetime asset base

It is important to review the investable assets needed to fund the remainder of a retiree's life. Many individuals today retire with large lump sums of investable assets through 401(k) or 403(b) qualified retirement plans. Retirees typically are allocating holdings across multiple asset classes while also managing liquidity for income needs. If markets decline dramatically in the first years following retirement, a wrong decision by a retiree could significantly impact future financial security just as retirement begins.

The optimal timing for asset liquidations and payouts is critical, and with many factors in flux during early retirement years, many retirees opt to start out with a more conservative investment approach than will be needed later in life. While it has been customary to realign portfolios away from equity toward fixed-income assets with age, this approach has evolved in response to increased longevity and the probability of spending more money in the earlier years of retirement.

Recent studies suggest that the best way to achieve a short-term defensive posture without sacrificing long-term growth is to trim equity exposure in the year prior to retirement and slowly reposition back to the asset class over time. Qualified retirement plans can play an important role in creating an optimal planning structure by facilitating what is known as an "asset location strategy." This strategy matches the tax characteristics of an investment type with the tax benefits of an account type. For example, the tax-deferred nature of qualified retirement plan accounts provides a safe haven for tax-inefficient alternative investments and high-yield fixed

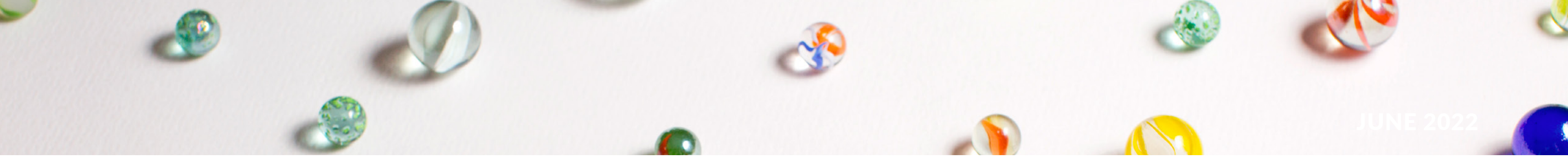
income. Nonqualified accounts, on the other hand, can be used to house tax-efficient investments such as qualified dividend paying stocks and capital gain property.

Family legacy and philanthropy

For retirees whose assets greatly exceed their anticipated needs, there is an additional bucket of wealth that requires a different analysis. These assets afford a much longer investment period and require strategies designed to limit and reduce future estate tax and generation-skipping transfer tax liabilities.

The use of an irrevocable trust where income is taxable to the grantor, for example, can be an integral part of the planning process. Passing the trust's income-tax liability back to the grantor provides the ultimate in wealth transfer through continued depletion of the grantor's personal taxable estate, while leaving the assets inside the irrevocable trust for future growth without causing additional transfer taxes.

In the case of philanthropic giving, there are many ways to optimize investment returns and realize tax efficiencies through gifts to charity. Understanding an individual's current and long-term tax situation will help determine the timing and type of the charitable transfer. If an outright transfer to charity is impractical, a more sophisticated vehicle such as a Charitable Remainder Trust allows an individual to retain current income from assets irrevocably set aside for charity. Conversely, a Charitable Lead Annuity Trust allows excess appreciation from a portfolio to be diverted to heirs after the charity receives a steady income stream for a term of years.



For individuals who enter retirement due to a once-in-a-lifetime event, such as the sale of a business, the transfer of a large charitable gift can maximize current income tax-saving opportunities while also allowing the individual to retain control of future charitable distributions through the use of private foundations or donor-advised funds.

Retirement should be a time to pursue our passions. For most people, the freedom to do this comes as the result of thorough financial planning. At Glenmede, our role is to help ensure you begin this chapter of life with a balanced cash-flow and asset plan in place that will allow you to realize your vision of the future.

PWEVG038-0622