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Can You Afford It?

By Ashlea Ebeling

Theodore and Ilene Bruccoleri of McLean, Va., are going to keep their 10-year-old Lexus SUV another year, maybe longer, and then splurge on a new red BMW 3 series coupe Ilene has had her eye on since she retired. It's not that they don't have the money to buy the new car now. "I'm not a pauper, but I've lived through a number of recessions," says Ted, 66, co-founder of executive coaching firm Human Capital Advisors and a former CPA. "I'm trying to conserve cash. You can never be too safe."

Cars, boats, trips, vacation homes, swimming pools, home upgrades, you name it. Pre-retirees and retirees (and their adult children) have lots of wants these days, but many are taking a step back and reassessing their spending—what they buy and when. That may not be great for the economy, but it is good for your family's welfare and your own retirement security.

Not everyone has got the new austerity religion of course. "Some people still want to keep up with the Joneses," says Dennis Klein, a CPA with Nussbaum Yates in New York City. "They still want the newest cars, the biggest vacations, the newest house. They have to look at themselves in the mirror and say, 'Can I really afford it?'"

If you want to be more cautious, but not deprive yourself of fun experiences and purchases you really can afford, here are some pointers and some examples to help you find the right balance.

1. Draw Up A Financial Plan

Start with a plan. "Everything from your basic needs up to your hopes and dreams has to go into your financial plan," says Kelly Campbell, a fee-based financial planner in Alexandria, Va. who counts the Bruccoleris as clients. "I always ask a new client, 'If I find out you're going to run out of money would you like me to tell you now or when you run out?' We joke about it, but it's important to see where you are now and where you'll be in the future because then you can make good decisions about how you allocate assets and cash flow."

In the Bruccoleris' case, they want a secure retirement for themselves and a "safety net" for their four adult children (this year they're helping with graduate school tuition for one and a condo down payment for another). "Parents' obligations never end from buying a bicycle to a car to a house—the stakes just get bigger," Ted says. But he's quick to note that he doesn't just dole out cash willy-nilly when his kids ask. He's taken his two older children to meet with Campbell and put together financial plans, and the younger kids will be next in line. "I want to teach them how to farm, so to speak. They want the latest technology, but they've got to save."

The Bruccoleris try to lead by example. So instead of staying in their large single family house, they have moved to a nearby condo for retirement and are reaping ongoing savings on real estate taxes and utilities.

2. Track Your Spending

You can have the fanciest plan you want, but it won't do you any good unless you keep track

of your spending to make sure that it is in sync with your plan. "A lot of people don't know actually how much they're spending," says Lyn Dippel, a fee-only financial planner with Financial Advantage in Columbia, Md. "Even if they do, there's a question of what's going to change in retirement." Some clients simply want to back into it, say they're making $200,000, saving $50,000, and paying $50,000 in taxes, that means they're spending $100,000 a year. But it's best if they take the time to list all the categories of expenses so they can go see where they're spending their money and where they might cut back.

Small changes that reduce your annual spending (and we're talking here about more than just passing up a daily Starbucks latte, although that helps), if sustained over many years, can make a bigger difference to your retirement security than simply passing up a one-time big ticket purchase. It may even mean an earlier retirement.

Dippel showed one couple with a $1 million investment portfolio who were spending $75,000 aftertax a year how reducing their spending by $8,000 a year would mean their nest egg would last five years longer in retirement. Another couple with a $2 million portfolio who were spending $200,000 a year cut back on expensive vacations, taking two a year instead of three. (Yep, they're still going to the Galapagos Islands this year.) They also stopped writing $13,000 checks to their adult children. The result was the husband was able to keep his planned retirement date rather than delaying it another two years.

3. Pick Your Toys Carefully

Calculate how much you spend on frivolous or extravagant items. Scott Tuxbury, director of retirement and investments with New Wealth Advisors in Tewksbury, Mass. pointed out to one client how much a motorcycle he never rode was costing him, about $2,800 a year in upkeep, insurance, and registration fees. "That one ride costs $2,800 a year. You put it that way, 'Oh,' the husband says, 'I'll ride with a friend,'" Tuxbury says.

Another guy, semi-retired, 52, and divorced, who got $3.5 million for selling a piece of his software company to a private equity firm, looked to Tuxbury for the okay to buy a $255,000 boat (after bragging that he bought his new girlfriend a $10,000 watch on vacation in the Cayman Islands). Okay, so he splurged on the watch. A plan is a living, breathing thing, and the guy has set aside a nice sum for one-to-three years out lifestyle expenses. The problem was that boat purchase was too big to come out of his short-term lifestyle splurge budget; he would have had to redeem shares to pay for it. Plus it would mean he could be out of money when he reached 88 based on predicted spending patterns. Solution: He found a similar boat, used, for $74,000, which he could afford within his long term plan.

4. Don't Let Your Home Become A Money Pit

When it comes to asking advisors "permission" before making big ticket expenditures, houses (and vacation homes) come up all the time. Dippel has clients who are postponing retirement for a couple of years and trying to ramp up their savings, but wanted to replace the windows and doors in their house, an $80,000 job. For now, after consulting with him, they are just going to do the windows. Also, when you're laying out your plan, plan for the unexpected. What looked like a straightforward reroofing job turned into reframing and reroofing, a $40,000 job, for one couple, and a leaky basement meant a foundation fix for an unexpected $30,000 for another couple, says Campbell. If you're considering luxury home renovations, check out the payback you're likely to get for various projects here.

When buying up or renovating to compete with the Joneses, remember that the bigger the house, the bigger the ongoing maintenance, repair and utility bills, says Jonathan Bergman, a financial planner with Palisades Hudson in Scarsdale, N.Y. But the nice thing about a fancy house, he notes, is you get to enjoy using it, and it will hopefully appreciate—although don't count on big value increases anytime soon.

Plus, a large home, and particularly a vacation home, can have a psychic payback as a place where multiple generations can gather. One Bergman client was spending $50,000 each summer for a one-month rental on Kiawah Island in South Carolina, gathering his adult children and grandchildren in one place. For that client buying a $4 million house on the island made sense. "Eventually I can see these folks moving there full-time," Bergman says. On the other hand, he nixed the purchase of a condo in Vail for a couple who like to ski there once a year. Instead they joined Exclusive Resorts, where they can try out $2 million properties around the world.

5. Keep Separate Accounts

For couples who fight over who spends how much on what, separate accounts can help break the tension and save cash, says Jean Dorrell, a certified estate planner in Summerfield, Fla. who works with retired and semi-retired folks living in The Villages and nearby planned retirement communities. One client, a 65-year-old anesthesiologist who still makes $100,000 a year, was tired of her 85-year-old husband telling her she puts the air conditioner on too low and she flushes the toilet too much. Now she pays the water and electric bills out of her separate account, and they don't have these arguments any more. "He is extremely conservative with his money and so was his first wife of 45 years," says Dorrell. Another variation on this: he plays golf too much; she shops too much. Answer: Get your separate income checks from annuities (or required minimum distributions from individual retirement accounts) put into separate accounts. Other income goes into a house account, for joint expenses.

Still, when it comes to jointly owned property, the discussions can get tricky. In another case, Dorrell had a husband who wanted to build a $35,000 swimming pool that his wife opposed. When she met with the couple, the husband brought in paperwork to have his wife's name taken off of their jointly held house so he could get a $75,000 reverse mortgage to pay for the pool, pay off the $25,000 they owe on their mortgage and take out the rest in cash. He's 69. The wife is 62. "They come to my office to try to solve the argument; he wants me to side with him so he can say, 'See, we can afford it!'" Dorrell recalls. But the husband left disappointed. "You both have to be on the same page,'' to make such a big move, Dorrell explains.

6. Just Say No

The Bruccoleris are keen on helping their kids, but believe there are times when you have to say no to avoid jeopardizing your own retirement. Campbell helped one retired couple deal with an adult son and his family of five moving back home after losing his job by having the son sign an agreement with mom and dad. He pays $1,000 a month in rent, and his wife and kids help with cooking and yardwork. Plus, he's promised to look his hardest for a new full-time job (and not just get by doing some consulting).

In a more extreme case, a widow in her 40s came in to CPA Klein with her son, a recent culinary school graduate who wanted $100,000 to open a take-out lobster roll restaurant in New York City. The widow has nearly $3 million in liquid assets, but also has two other younger kids to care for as well as her own retirement to fund. "I believe he thinks there's an open checkbook," Klein says. "She's trying to be nice. I'm taking the role of the bad guy." The kid came in with a lease in hand (the deposit for five months rent is $55,000) but without a bid from a contractor of what it would cost to build out the place, and uncertain about the cost of lobster. "I've implored them not to sign the lease until they get the numbers," Klein says. His parting advice applies to all big spenders. Before you write the check, ask yourself: "Is this with the heart or the head?"