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Money Milestones

# Retirement Catch-Up: How To Start In Your 50s

William P. Barrett, 03.16.10, 6:00 PM ET

OK, you're in your 50s and still have a job--maybe even a decent one--but the amount of savings you've put away for retirement is squat. Zippo. Nada. Is there any way you can avoid an impoverished old age or working until you drop?

The answer, fortunately, is yes. Even those getting a tardy start in thinking about retirement can take advantage of tax breaks and other moves to make up significant ground. This may require substantial changes in one's lifestyle now, but they're almost certain to be less painful than what might be required in 10 or 20 years if you don't start now.

"It's not too late unless you think it is," says Andrew Hudick, a financial planner in Roanoke, Va., who regularly sees clients needing to play retirement catch-up.

**In Pictures: Retirement Planning For Late-Starters**

The most important first step to take is to start saving. Now. Even if you haven't yet worked out any kind of a plan; that can come later. But you're still going to need the money.

We're not talking about the kind of piddling savings that comes from giving up your twice-a-week Starbucks Venti Latte. Instead, you need to start saving a good 10% of gross income or even more. There essentially are two ways to save. One is to pay down high-interest-rate debt that isn't already tax-deductible--especially credit cards. If you're paying 20% on credit card debt, in effect you get an immediate 20% return for every dollar you pay off.

The other way, of course, is to put funds away. This is where the tax code comes in. Take full advantage of your company's 401 (k) plan in which contributions are excluded from your current year's income. It's nice but not crucial if the employer matches part of the contributions. In a 25% bracket, a $10,000 contribution by you reduces your taxes by $2,500. Federal law allows workers who will be 50 by the end of the year to salt away up to $22,000 of their own contributions, pre-tax, for 2010. Investments in such retirement funds grow tax-deferred until they are withdrawn, at which time they are taxed at ordinary rates. While tax rates may go up overall, your own rate is likely to be lower in retirement, particularly given the late start you're getting on savings.

If your employer doesn't have a 401(k), open an individual retirement account at a mutual fund company or brokerage. Those who don't have any employer pension plan can put away up to $6,000 pre-tax a year. If you do have a current employer pension plan, no matter how crummy, then you can only deduct the full contribution if your modified adjusted gross income is $89,000 or less for a couple, or $55,000 or less for a single. But you can make a $6,000 per person nondeductible contribution to a Roth IRA with modified adjusted gross income of up to $166,000 per couple and up to $105,000 for a single. (A Roth grows tax free, and all withdrawals in retirement are tax free.)

You can also fund tax-advantaged retirement savings with income from a second job or side business--a good thing to build up now, since you'll want to continue earning something in retirement. Say you're making $5,000 a year selling hand-made jewelry on eBay. You may be able to put it all away pretax in a Simple IRA or other special savings plan for the self-employer. For details, click here.

How should you invest your retirement funds? Most 401(k) plans have a number of mutual-fund options, and money in an IRA can be invested almost anywhere. Due to the continued volatility of stock markets, Hudick recommends for starters low-cost bond funds, in which the chance of a loss of principal is minimal. The last thing you want is to see the disappearance of 20% of your portfolio in the next stock market bust. As your nest egg grows larger, you'll want to look more closely at what percent you want to invest in equities--preferably low-cost index mutual funds.

Perhaps the biggest problem in starting a retirement plan later in life is the loss of a prior significant period of time over which earlier investments could have compounded and grown. At a 5% rate, an investment doubles in 15 years; at 4%, in 18 years. But even if you're in your 50s, you can still take advantage of the magic of compounded returns. That's because--actuarially, anyway--your retirement is likely to run upwards of 20 years. That's a long-enough period for investments you put away today to bear fruit.

As you get the savings going, you should figure out where you stand financially and what you'll need. Even if you aren't the sort to track every nickel spent on Intuit's Quicken, it's not hard to draw up a family net worth statement listing all assets and liabilities, and an income statement showing income and expenses over the last year. Data on your latest tax return can help.

There are all kinds of rules of thumb about what level of your current net income you'll need to sustain yourself in retirement, generally ranging from 60% to 80% to even more. But if you're new to retirement savings, don't be paralyzed because you won't reach those goals. Simply do the best you can and keep in mind that you're not starting from zero.

For example, even if your current employer doesn't offer a traditional defined benefit pension plan--one that pays a set amount each month--you may well have earned a monthly stipend from a previous job. This is a good time to paw through your old files and find records of any pensions from ex-employers you may be entitled to.

Even more significant is Social Security, which replaces 42% of the salary of a median wage earner who retires at the "full" or "normal" retirement age--66 for those who were born between 1943 and 1954. Replacement rates are higher than that for low-wage workers and lower for high earners. Plus, the replacement rate is higher for one earner couples, when spousal benefits are factored in.

Every dollar that comes from Social Security is one less dollar you otherwise have to provide for. You can get online an official estimate of your benefits from Social Security. Given the federal deficit, younger folks might rightly worry they won't get what they're promised from Social Security. But those 55 and over are unlikely to be nicked too much by any Social Security changes, unless they have a fairly high income.

You can start drawing early retirement benefits from Social Security at age 62, but it pays to wait, especially if you continue working past that age, and is crucial if you've begun saving late. Delaying the start of Social Security benefits until age 70 can boost the monthly payout by as much as 80%. For more on how to get the biggest Social Security payout, click here.

Here comes the tough-love part. If you seem to have no money left over at the end of the month to put away one way or the other and you don't want to get a second job or work longer, you're going to have to reduce your style of living. It's as simple as that. Sure, there's a lot of nickel-and-dime stuff many people can do--eat out less, buy used cars and so on. But you'll have to tackle the big stuff. Consider downsizing to a smaller, cheaper and less-expensive-to-operate house or even renting an apartment. (The first $500,000 of any gains on a principal residence sold by a couple is tax free, meaning more to invest now.) Even more dramatically, ponder relocating in retirement to an area with a significantly lower cost of living. Tell the grown children still living at home they're going to have to start fending for themselves.

It doesn't take a lot to start building that nest egg. In a tax-deferred account and figuring a 4% annual return (compounded monthly), putting away just $500 a month would produce $74,000 in 10 years. That may not seem like much. But at current rates, for a couple that would be 68 years old then, that sum would buy an immediate annuity paying out $433 a month until both spouses are dead.

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