**The Bucket Plan: Protecting and Growing Assets for a Worry-Free Retirement**

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Retirement today presents unique financial planning challenges worldwide. The responsibility to navigate volatile global markets, taxes, inflation, and increasing life expectancy falls on individual investors or their financial advisors. Investing too safely can result in clients losing purchasing power due to inflation; investing too aggressively can expose a client to significant financial loss. Both scenarios can create the risk of a client running out of money prematurely in retirement. Additionally, investors have traditionally fled to what they perceived to be a “safe” investment in bonds. With interest rates at historical lows in many leading global economies, if interest rates increase, investors may find that their so-called safe haven is a glass house.

These examples illustrate the three biggest dangers facing retirees today: market risk, interest rate risk, and sequence of returns risk. Advisors without a clear understanding of these dangers cannot effectively serve their clients. Advisors who do understand these risks have a massive opportunity to protect their clients and create a client relationship for life. No matter where you live—the Americas, Asia, Europe—all of these risks can, and likely will, impact your clients and their chances for a successful retirement, unless you help them to address it in advance.

The good news is there is a way to mitigate each of these potential risks by segmenting or compartmentalizing money into three different buckets based on a client’s investment time horizon, volatility tolerance, income need, and, domestically, tax qualifications utilizing The Bucket Plan. [visual]

Even though the name may imply buckets, The Bucket Plan is not solely meant to “bucket” a client’s money for different types of expenses, but rather to compartmentalize and structure assets appropriately to create a long-term, worry-free plan for retirement. The Bucket Plan is quite simply an asset-positioning philosophy. It efficiently ensures liquidity, maximizes potential income distributions, minimizes taxes, eliminates sequence of returns risk, maximizes growth opportunities, and ensures that certain risks associated with behavioral finance—or people making uniformed financial decisions based on their own personal emotion—are minimized. We accomplish this by establishing three phases, or buckets, to the plan—the short-term, the mid-term, and the long-term.

Let me explain. [visual]

**Bucket 1:** The “Now” Bucket is designed to be safe and secure money and to be used to cover living expenses in the first year of retirement as well as larger planned expenses such as a new car or home repairs. It’s also an emergency fund in case unexpected expenses arise. This bucket is protected from market fluctuations; however, returns will be minimal and likely not keep pace with inflation, so we don’t want to have more money than necessary in the Now Bucket. This is typically the money in the bank.

**Bucket 2:** The “Soon” Bucket is the preservation bucket. This is the money that we may need to access sooner rather than later, so it should be invested for growth, but conservative growth. By choosing conservative investments, average returns should be expectedly higher than in the Now Bucket. This growth helps offset the rising costs of gas, groceries, and other daily living expenses, providing a baseline of income and an inflation hedge where we can draw a little more as the years go on and things get more expensive. And, by investing conservatively, you avoid the risk of taking out money at a market low, or sequence of returns risk, as this account should not be exposed to extreme market fluctuations. This bucket may be accessed for periodic distributions needed for additional money outside of the Now Bucket, or it may provide income in the first phase of retirement. Insurance is widely used in this bucket to provide both security as well as consistent income for this phase of retirement.

If clients are younger or have a long time before they want to retire, this would be any money they could access penalty free if they needed to access assets outside of the Now Bucket, or the first bucket.

Our first goal with the Soon Bucket is preservation. We want to work to mitigate the potentially catastrophic damages that market volatility or sequence of returns risk could have on the value of the account. For a conservative client, this account might be composed of 100 percent fixed or low-risk investments. For a client who is comfortable with taking a bit more risk, this money can participate in the market but needs to be invested conservatively to preserve the account value. Rather than allowing a down market to force our clients to change their lifestyle or retirement time lines, the Soon Bucket’s conservative investments help insulate from major market corrections. This helps avoid pulling money out of investments when the market is down. The Soon Bucket should also include an inflationary hedge to ensure that if the client is drawing from this bucket during the first phase of retirement, we have enough funds to also be able to increase the income to keep pace with inflation.

**Bucket 3:** The “Later” Bucket is designed for long-term growth and legacy planning. Now that we have bought the client a time horizon with the money in the Now and Soon Buckets, we turn to the Later Bucket. Since we know we will not need to draw any money from this bucket until the later years of retirement (generally 10 years or longer), we can confidently invest this bucket in more long-term, growth-oriented investments. As the Soon Bucket is spent down over time, the Later Bucket will be used to replenish those assets. We do this in one of two ways, or a combination of both: market growth in a low-cost diversified managed portfolio for those investors comfortable with some risk in this bucket, or a guaranteed lifetime income (pension annuity) to create an income floor for a more conservative client.

Because of the healthy time horizon established with the Now and Soon Buckets, clients can feel comfortable about committing a portion of their assets to those longer term vehicles in the Later Bucket. In addition to growth and income, it is critical to educate clients on long-term care, disability, and legacy planning in the Later Bucket as well. It’s typically in the later years of retirement that the risk of long-term care or disability expenses is at its highest, and ensuring we have enough to cover these expenses is critical in building this comprehensive plan. Also, not many people realize that legacy planning, or what to do with the assets and estate after one spouse passes away, isn’t just for the children but for the surviving spouse. When one spouse passes away, the household income often goes down and taxes can go up. This later bucket helps to plan for these scenarios so there would be no surprises financially if or when one of these types of events occurs.

So, to recap, the Now Bucket provides for an emergency or comfort fund and covers planned expenses on the horizon—it’s the safe and liquid money. The Soon Bucket provides an income source to a person during the earlier years of retirement. It’s the conservative investments and income money. It buys a time horizon to invest money in the Later Bucket for growth so inflation doesn’t derail one’s long-term retirement plans. Each phase has a different time horizon, so each phase has a different volatility profile—we’re going to discuss that in more detail later on.

One of the unique things we do before we get started taking a client through the planning process is an exercise called the Initial Concerns Ranking Worksheet. [visual] This exercise ensures we are focusing on their priorities and not ours.

We have them rank their top concerns from one to three. One is “I was very concerned about it. It’s a top priority.” Two is “It’s important, but it’s not a number one.” Three is “Not at all, not even on the radar, not a concern.” It gives us phenomenal insight into clients and what they’re thinking and what their priorities are, because too often we, as planners and advisors, get too caught up in our own agenda, when really what we need to be doing is making it all about them. That’s what this worksheet is all about. Facilitating this conversation as you do this with clients is very powerful, especially when you get to the end of the meeting and you can go back to those number ones and reinforce why they need to hire you as their planner, their advisor, and to take them through this process. With this information in hand, you can start them on The Bucket Plan process.

When you approach bucket planning with the concerns in mind, you can be truly strategic in advising clients on the financial solutions that will help maximize and preserve their wealth while focusing on minimizing controlled risks, such as market volatility, sequence of returns risk, inflation, taxes, longevity, and estate transfer.

There are six steps and tools to The Bucket Plan planning process to use with your clients to come to a final plan and recommendation. They are:

1. *The Money Cycle*: Educate your client on the three phases of the money cycle, along with the biggest mistakes we see clients make—skipping the preservation phase.
2. *The Bucket Plan Presentation*: Package a financial plan in terms clients can understand.
3. *The Asset Sheet*: Gather comprehensive information about their liquid investable assets segmented out by tax qualification.
4. *The Income Gap Assessment*: Determine the “income gap” between retirement income sources and retirement income needs.
5. *The Volatility Tolerance Analysis*: Discover the appropriate amount of risk clients are comfortable with in each bucket to make suitable recommendations.
6. *Design The Bucket Plan*: Pull all the pieces together to create their own version of The Bucket Plan.

Let’s start with the money cycle. The money cycle is the way that we explain sequence of returns risks. Simply put, this is the danger of having investment losses early in retirement and having to pull from those investments for income while they are down. Once those losses are realized, you can never make that money back. You can have a very negative outcome at the end of your retirement if you experience a downturn early in retirement and you’re drawing off those assets.

The money cycle consists of three phases: the accumulation phase, the preservation phase, and the distribution phase. Accumulation begins as soon as one starts earning a living. These are the earning, saving, and investing years of people’s lives. They have a long time horizon before they need those assets and can afford the volatility and the ups and downs of the market because, let’s face it, if they lost the money, they’re still working; they still have plenty of time to make it back. The preservation phase begins five to ten years before retirement, where people need to start reducing the risk they’re taking on with their savings and investments and begin preserving their wealth for retirement. It’s very important to preserve a portion of that money to draw off of throughout the first phase of retirement. And, finally, the third phase is the distribution phase, where people take distributions from their accounts for income in retirement. This is distribution to ourselves in retirement and distribution to our family upon our passing.

What we most often see, though, is that people go from the accumulation stage and directly into distribution. Too often they continue to invest the money as if they’re preparing for retirement, or it’s a long way out when they’re already retired or about to retire. The biggest mistake people make is to continue or be invested as if they’re in the accumulation phase, when they’ve actually gone into a distribution phase or are about to.

This sets up the conversation for The Bucket Plan philosophy. The Bucket Plan is an asset-positioning philosophy. Again, the objective of this is to segment your money based on the time horizon and the purpose of that money. We have a video that helps to explain The Bucket Plan philosophy.

We use this video to quickly and simply explain the philosophy. Once they’ve viewed it, I would explain an overview of our approach to clients. It would sound something like this:

 What we do is we subscribe to a simple, three-bucket approach. The difference that you’re going to see is in this middle bucket, the Soon Bucket. That is your preservation money that you’re going to draw off of throughout the first phase of retirement. The Now Bucket is your safe and liquid money. It’s the money you’re going to keep in the bank. You are not going to invest this money. You’re willing to sacrifice the rate of return you’d otherwise earn if you were to invest the money to have it completely safe and liquid. And the Later Bucket is your long-term money. This money can stay invested and continue to grow to protect against inflation for the later years of retirement.

If you’re already retired or about to retire, we’re going to put up to 12 months’ worth of income in that bucket to buy that first year’s worth of income for however much we’ll need to draw off your liquid investible assets. In addition to that, we want to make sure there’s an emergency or a comfort fund, a certain amount of money that’s going to give you the peace of mind to put your head on the pillow at night, to know it’s sitting there in checking and savings. Everybody has a certain magic number. We’re going to help you come up with that number and make sure that money is there in the bank. Then, lastly, are planned expenses. Any large planned expenses you have on the time horizon in the next few years, we want to set that money aside. We don’t want to invest it. We don’t want to tie it up. We don’t want to subject it to market volatility, because if we’re going to need that money soon in the Now Bucket, we want to go ahead and put it there and make sure it stays in liquid.

Once we’ve established a Now Bucket, it’s a simple, two-bucket approach for the future years: the Soon and the Later Buckets. The Soon Bucket is the money that you may need sooner rather than later. It’s the money that you may need to draw from throughout the first phase of retirement. It’s maybe the money that you might need to take a required minimum distribution from if you have those types of accounts, or it’s just that money that you want to take a more conservative approach with in case you need to take withdrawals sooner rather than later. We don’t want to subject it to the volatility and ups and downs of the full swing of the market, because if we were to need that money sooner rather than later and the market was down, we’d have to sell out investments, and we’d never be able to make that money back.

By establishing a Now and a Soon Bucket, we’ve bought ourselves a time horizon to confidently invest the rest of the money in the Later Bucket. The Later Bucket’s purpose is long-term growth and legacy planning.

When I get to legacy planning, clients might say, “Jason, you know what? My kids are raised. I’m not worried about it. Whatever is left is left.” How many times have we heard that? I would say, “But, see, legacy planning is not just for the kids. Legacy planning is, most importantly, for the surviving spouse, because when one spouse passes away, have you ever considered what happens to the income? If that spouse is working, or if they’re both on social security or another form of fixed income, one of those income sources could be reduced or eliminated when one spouse passes away.” And, at least domestically, taxes can increase when one spouse passes away too. When married, filing jointly, you have double the standard deduction, double the personal exemption. That gets cut in half for a single filer, a widow, and so now not only does your income go down due to loss of fixed income or income from work, but, in addition to that, taxes can go up for the surviving spouse because you lose a couple of the biggest deductions and all the brackets shrink. For the same amount of income, you can pay up to 66 percent more tax liability for the surviving spouse for that same amount of income.

We explain this three-bucket approach, and the main two things we’re trying to communicate are the importance of having that preservation bucket, that Soon Bucket, and they’re going to have a realization that they probably don’t have a Soon Bucket, and then the Later Bucket. No one has ever talked about legacy planning for the surviving spouse; it’s a very powerful conversation.

Now we’ve explained the money cycle, and we’ve created the need. In The Bucket Plan philosophy, we talked about the solution. Throughout the next steps of the process, we gather the information that we need to be able to build a retirement income plan for these prospective clients, on paper and without the need for software.

The next step in The Bucket Plan process is an asset sheet questionnaire. The clients bring in all their financial documents, and we document everything in the asset sheet questionnaire. This includes the beneficiary designation information, the cost basis information, debt and any tax liability they’re going to have on pretax and post-tax investments, the asset titling information—we want to see if it’s going to avoid probate or if you’re going to subject your clients to have to go through that lengthy process of probate. We’re going to plant some seeds on what’s working and what’s not in their current financial plan for retirement. We’re going to identify what that liability is throughout this asset sheet questionnaire, but, most importantly, we’re going to get all the relevant information, all the documented information, to make the most appropriate recommendations that are in the client’s best interest.

Then, step four is the income gap assessment. The income gap assessment is a very simple tool to help determine what they have for income sources and what they’ll need to supplement the difference for income needs in retirement. [visual]

If clients are retiring in the next five years or are already retired, this is a very appropriate tool to use and much more efficient to get to the income gap, or the number that you need to build in their plan. In the first section, we’re identifying the current amount deposited into checking—net income after taxes. So we’re looking for the net after-tax income that they’re receiving and living off of in their checking account. In this case, Jerry and Irene were both working. This is what they were living off of: $57,000 a year total between the two.

Now, asking the question, “If we could replace the same amount of income you’re living off of now, and you could have that same income in retirement, would that be sufficient?” most people are absolutely going to be able to live off of what they’re currently living off of now. Some expenses go up a little, some may go down a little bit, and we’re going to make those adjustments during this exercise.

The second category is the fixed income in retirement: pensions, social security, anything that they’re going to be able to rely on throughout the rest of their life in retirement—fixed monthly income sources. In this example, they both were going to get social security—that’s $20,000 a year. So we have a $57,000 annual income; $20,000 is offset by social security. Now, the third section is adjustments, any major expenses that are changing in retirement, anything going up, anything going down.

They might have a huge travel budget. They might have additional tax liability. They might be paying off a lake cabin like in this example. This is where you make your adjustments. In this example, they’re paying $1,000 a month for a mortgage, and that’s going to be gone, almost paid off, and so $12,000 a year is going to be going away. If we take the $57,000 and back out the $32,000 (social security and mortgage payment), we have our income gap of $25,000 a year. So it’s a nice form to create a shortcut. That’s our income gap assessment.

The next section we’re going to talk about is volatility tolerance analysis and designing The Bucket Plan. The volatility tolerance analysis is a two-pronged risk assessment questionnaire, so we can be sure to stay within their investment comfort zone for both the Soon Bucket and Later Bucket. These dollars have different purposes and time lines for accessing the money—one risk profile won’t work for both—you need an individual risk assessment for each bucket scenario. So the Soon Bucket has its own scoring, and the Later Bucket has separate scoring. Taking someone through this entire questionnaire is about a 10-minute process. It’s not a lengthy process, but at the outcome of it, they’re going to have told you how conservatively or aggressively they want to invest in their Soon Bucket separately from their Later Bucket, because different time horizons, different purpose of the money.

It’s very important to score the buckets separately. In this case, the Soon Bucket scored a stable category, the Later Bucket scored a growth category, so now we have a better insight of how they want their money invested respectively in each of these buckets. [visual]

The last step to the process is designing their Bucket Plan.

One thing to note: When describing The Bucket Plan, it is impactful to have the Now, Soon, and Later Buckets drawn on an electronic whiteboard (I use the Panaboard made by Panasonic) and to give an overview of the process. Showing the visual on the board has a powerful effect, because clients can easily see that they don’t have anything like this in their current retirement plan. I describe some of the biggest mistakes I see people make and show how The Bucket Plan helps avoid them. For example, many people who are ready to retire continue to invest their money as if retirement is many years away. They have Now and Later Buckets, but never set up that all-important Soon Bucket (which should be much more conservatively invested) containing the money they will draw off of in the first phase of retirement. That’s just another disaster waiting to happen.

In the Now Bucket, we’re going to facilitate a conversation on what Jerry and Irene’s magic number is. Remember, we said everybody has a “put your head on the pillow and sleep at night” magic number, an emergency fund. In this case, $35,000 is what they said they wanted in their emergency fund, always kind of sitting there safe and liquid, not going to be used for income or planned expenses. When we talked about planned expenses, they wanted to trade in their current car and upgrade their car, and they wanted $15,000 that they would need approximately to put down. They didn’t want car payments, so $15,000 was the planned expense component. In this case, they were not retiring for two to three years, so we did not need to put up to 12 months’ worth of income in the Now Bucket, only the emergency fund and only the planned expenses. So we have a total of $50,000, and that is going in the bank.

In the Soon Bucket, we have Jerry’s IRA. How much was that income gap? $25,000, remember? What we do is very simple and simple for the client. I like to try to keep everything very simple. Too often we get caught up in our own industry lingo and how to do things, but if we simply buy a 10-year time horizon in the Soon Bucket, meaning to fund 10 years of income, we can let the market do what it does in the Later Bucket. So, $25,000 a year times 10 years is $250,000. We’re going to use Jerry’s IRA money to fund this, because, in doing our due diligence, we recognized that we’re going to be able to draw off those funds with little to no tax liability because their only other source of income was social security. So we’re going to draw off Jerry’s IRA. And because milk, bread, gas, eggs, and everything gets a little more expensive as time goes on, we’re going to be able to draw a little bit more every year to keep up with inflation. So we’re going to put an inflation hedge in there by including some of Irene’s IRA as well.

Those are the two components that make up the Soon Bucket, and we’re using IRA money to start to diffuse or spread out that tax liability of these pretax retirement accounts that could potentially be taxed at a higher rate in the future. We’ll leave the money with a lower tax liability in the Later Bucket for the surviving spouse and the family upon their passing for tax-efficiency purposes. In addition to that, we know we’re going to have required minimum distributions start to come into play during the next 10 years, so by using a portion of Jerry’s and Irene’s IRAs, this income will cover those requirements as well.

That puts the total here for the Soon Bucket at $312,500. One of the questions we ask on the income gap assessment is “Is there a portion of your money, or a percentage of the money, that you want guaranteed?” In this case, they wanted to have their baseline income guaranteed, but were willing to invest the inflation hedge money in a very conservative portfolio or stable portfolio, so we used an annuity to guarantee the income of the $25,000 a year to buy the 10-year time horizon, and then a stable portfolio for the remainder of the Soon Bucket.

In the Later Bucket, we have the remainder of Jerry’s IRA, the remainder of Irene’s IRA, and then they have a joint nonqualified account of $365,000. Remember, just like they scored stable in the Soon Bucket on the volatility tolerance analysis, in the Later Bucket they scored growth, so that remaining $502,500 we invested in a pretax growth portfolio for the two IRAs and a tax-managed growth portfolio for the nonqualified accounts for tax efficiency with loss harvesting with the nonqualified money, so we don’t have a bunch of dividends and interest and long-term and short-term capital gains showing up on their tax return.

And that’s how you build The Bucket Plan. Let me summarize some of the main parts to this construction process. The Bucket Plan identifies clients’ comfort level of risk in each bucket and gives you a full picture of all their investable assets so that you can provide holistic and thorough financial advice with a keen eye toward tax efficiency. And, through the planning experience and sequential steps, it simplifies the client experience, giving them the knowledge, comfort, and confidence to move forward with your recommendations.

The Bucket Plan also provides a tangible deliverable to clients—further differentiating you from “other” advisors, agents, reps, and planners, who are simply selling products, as well as providing clear documentation you can easily revisit to keep clients dialed in to why their plan is built the way it is built over time and for regulatory auditing protection purposes.

The Bucket Plan is all about educating the client, so The Bucket Plan recap is a great time to go over the three principles of sound investing to help affirm that your efforts are aligned:

1. *Time Horizon*: The first principle is the time horizon. By creating Now and Soon Buckets, you’ve bought clients sufficient time to grow the money in the Later Bucket.
2. *Volatility Tolerance*: The second principle is risk tolerance. We want to set clear expectations with clients to avoid taking on too much or too little risk. That’s why we are going to complete a two-pronged volatility assessment so we can be sure to stay within their investment comfort zone for both the Soon Bucket and Later Bucket.
3. *Diversification*: The third principle of sound investing is diversification (don’t keep all your eggs in one basket). By now, clients can clearly see the thorough measures you are taking to provide these three investment principles.

When you sit and sketch out an individual Bucket Plan, going through these exercises, you are walking your client down the path to a stark realization: His or her assets are not properly allocated—and *you* are the professional to help make it right.

One of the most important things to remember is to keep it simple. At a certain point in our career, and once we have a certain level of education and experience in this industry, it can become easy to overcomplicate things for clients. That’s another benefit of using The Bucket Plan to frame out a client’s financial or retirement income plan. It’s a simple way to communicate a complex topic.

Next, we have an interactive exercise that you can have clients and prospects complete to help them understand why they need a Bucket Plan. We have The Bucket Plan scorecard to help clients rank themselves based on what they do or don’t have adequately prepared or in place for retirement, and at the end of the exercise it becomes obvious that there are a lot of gaps in their current financial plan.

The scorecard ranks from 1 to 12, with 1 being the least prepared and 12 being the best-case scenario for each area, with a number of options in the middle. [visual]

The first statement is “well-coordinated team of professionals,” and clients would answer on a scale from 1 to 3 if they “don’t have a team, but I’m sure I can figure this all out on my own when I need to.” They would answer between 4 to 6 if they “get some tax help and investment advice, but there may be some gaps in my plan.” They would score from 7 to 9 if they “have an accountant, advisor, attorney, and insurance agent, but they don’t coordinate with each other.” And, lastly, they would score from 10 to 12 if they “have a full financial, tax planning, and legal team, and they all work well together.”

You will continue to do this for each of the eight statements in the left column: proactive income tax planning, health care expense funding planned, legacy planning and documented organization, a documented financial plan that’s fully understood, assets are segmented based on time and purpose, stable and sustainable lifetime income, and peace of mind.

This will help illustrate where you or your clients are in developing a well-orchestrated plan for retirement. Clients who score less than 80 have some serious gaps that must be addressed.

For additional reading on this topic, I invite each of you to read my newest book: *The Bucket Plan: Protecting and Growing Your Assets for a Worry-Free retirement* that shares a step-by-step appointment process, based on a true story of real clients of mine. It is told as a fable through their perspective—what questions they ask, what conversations we had from start to finish about building the financial plan of the same case study we have introduced here today.