How to Prepare for Your Retirement

A GUIDE TO:

Getting Ready to Retire

EDUCATION GUIDE

THE Vanguard GROUP®

Create a plan now for a more comfortable retirement

If you're five years or less from retirement, now is the time to start consulting with your financial advisor, who can help you develop a plan for managing your assets when you finally retire.

This guide will help make consultations with your advisor more productive, while providing information to help you better understand his or her recommendations.

Step 1: Your Retirement: When, Where, How?

Step 2: Your Expenses

Step 3: Your Income Sources

Step 4: Your Investment Mix

You're almost there!

Soon you'll embark on one of the biggest changes in your life—the transition to retirement. Whatever way you choose to spend your newfound freedom—traveling, golfing, volunteering, or even working part-time—you have some important financial decisions to make first.

Your financial advisor is ready to guide you through the process.

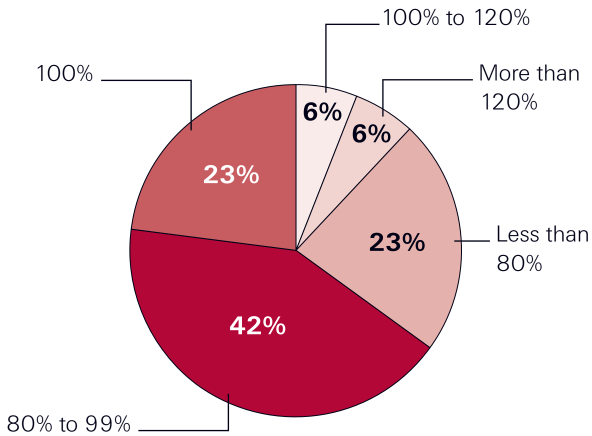
For the first time in your life you'll be spending your nest egg instead of building it. Are you ready to take that step? Do you know how much you'll need in order to maintain the lifestyle you want? Your financial advisor is ready to guide you through the process, helping make sure your assets are managed properly, so you can enjoy the comfortable life you've worked so hard to create.

Some careful preparation over the next few years can help you stay on the road to the retirement you've planned for.

Step 1 Your Retirement: When, Where, How?

To create your financial plan, your financial advisor will need to know some basic things about your intentions for retirement. You should make some decisions now about when you want to retire, what you want to do in retirement, and—importantly—estimate what it's likely to cost.

High-Net-Worth Expected Retirement Income as a Percentage of Current Income



Average surveyed household aged 57 with an average net worth of $3.3 million.
Source: 2004 Phoenix Wealth Survey.

As the chart on this page shows, 35% of high-net-worth investors expect their retirement income to be the same as or greater than their income during employment. They consequently believe they can finally do all the things they've dreamed of doing, without concerns about spending. However, when they sit down with their financial advisor and "do the numbers," many find that this isn't a realistic expectation.

It's important for your advisor to understand your retirement goals, so he or she can help you develop a financial plan that seeks to provide comfortably for your needs, but is sustainable over the many years you are likely to live in retirement. Working with your advisor, you may find you'll need to adjust some of your expectations.

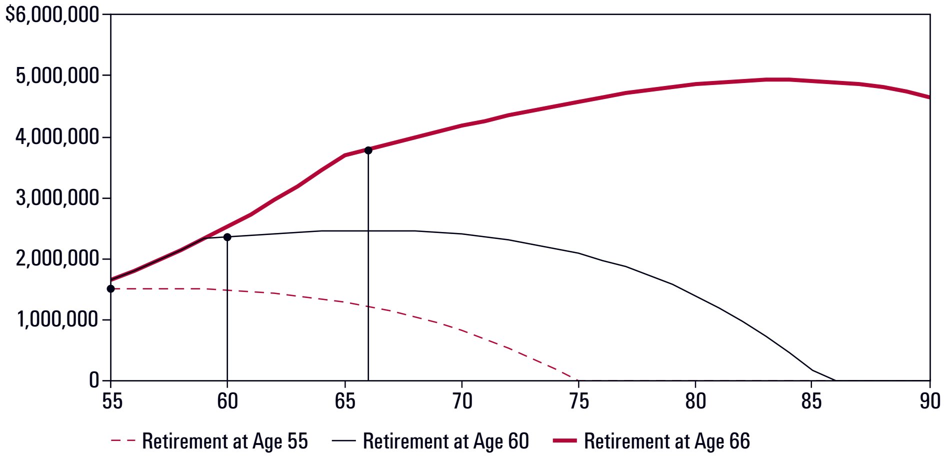
When Do You Want to Retire?

The age at which you retire can have a huge impact on how long your retirement portfolio will last. The chart on this page shows projected savings at ages 55, 60, and 66, and how those savings might decline over time, depending on when you choose to retire.

In this hypothetical example, a 55-year-old retiree who expects to spend $175,000 in his first year of retirement might run out of savings before he turns age 75—unless he reduces his expenses. If he waits until age 60 to retire, he could start out with more savings, but the impact of inflation might mean he'll need $202,873 to buy what $175,000 had bought five years earlier. Nevertheless, retiring at 60 could mean his savings could last until he reaches age 85. However, if he retires at age 66, his savings could last his entire lifetime and then some.

To help create a comfortable lifestyle through your entire retirement, work with your financial advisor now so you're well prepared. And remember, investment returns are not guaranteed, and the value of your investments can fluctuate.

The Impact of Retirement Age on a Hypothetical Retirement Portfolio



This hypothetical example does not represent the return on any particular investment and assumes:

- A nest egg of $1.5 million at age 55.
- From age 55 through ages 60 and 66, ongoing contributions of $14,000 per year to a 401(k) plan that has a 6% employer match, plus additional contributions of $25,000 a year to a deferred compensation plan.
- A pension of $75,000 a year if retirement is at age 55 increasing to $93,253 annually if retirement is at age 66.
- An increase in Social Security benefits of 2% per year.
- A 6% average rate of return on investments.
- Expenses beginning at $175,000 a year at age 55 and increasing with inflation at an average rate of 3% per year.

Step 2 Your Expenses

Once you've decided on your retirement date and considered what you want to do in retirement, your financial advisor can help you determine how much your retirement is likely to cost. We've included a worksheet on page 12 to get you started.

Many retirees spend more money in retirement than when they were working.

How Will You Spend Your Money?

Sit down with your spouse and financial advisor and make a list of all your projected retirement expenses. Categorize your expenses as nondiscretionary (necessary items such as mortgage payments, utilities, and food) or discretionary (optional items such as travel, hobbies, and entertainment).

Many retirees find that they spend more money during retirement—especially on things like travel, hobbies, and entertainment—than they did while they were working. In addition, you may have to cover expenses for health care or prescriptions that are now paid for by your employer's insurance plan. And you may also find yourself incurring costs to care for an aging parent.

Contact your employer's benefits office to obtain a list of the benefits you are receiving now and those you will receive after retirement. Your advisor will use this information to determine which benefits you will need to replace or supplement.

People Are Living Longer

As you estimate your expenses, keep in mind that people are living longer in retirement. As you can see in the table on this page, there's a good chance that either you or your spouse will live to age 90. This means your portfolio may have to last for 30 years or more, depending on when you retire.

Plan for Inflation

Inflation can have a significant impact on the value of your investments. Since the 1920s, inflation has averaged about 3% a year,* but there have been periods when it has been much higher. Even at an inflation rate of 3% a year, you'll need about $270,000 in 20 years to buy what $150,000 buys today.

Life Expectancies at Age 65

Age	Husband	Wife	Either Spouse
70 years	92%	94%	99.5%
75 years	80%	84%	97.0%
80 years	63%	71%	89.0%
85 years	41%	53%	72.0%
90 years	20%	32%	45.0%
95 years	6%	13%	18.0%
100 years	1%	4%	5.0%

Source: Society of Actuaries Retirement Participant 2000 Table.

*Source: The Vanguard Group.

Health Insurance

If you are planning to retire before age 65, health insurance could be a significant expense that your advisor will need to factor into your financial plan. You may need to supplement your employer-provided medical plan or perhaps even provide your own health insurance until you reach age 65 and qualify for Medicare benefits.

After age 65, most people use Medicare as their primary health insurance, but there are costs your advisor will need to consider, such as the monthly Medicare fee, co-payments, and deductibles. Medicare also does not currently cover most prescription drug costs, routine physical exams, most dental care, or routine eye care. However, Medicare does provide a prescription drug discount card that may reduce some prescription costs, and is scheduled to offer a prescription drug benefit for the first time in 2006.

Your advisor also may talk to you about expanding your Medicare insurance options. Because of the limits on medical expenses that regular Medicare covers, many states provide the option for retirees to join a Medicare-related, managed-care plan that increases your coverage. However, these plans usually limit your choice of doctors and hospitals. If you need more coverage or want more choice than these kinds of plans provide, you may also purchase supplemental insurance known as Medigap, to fill the "gaps" in Medicare coverage.

Whatever type of coverage your advisor helps you select, this cost must be taken into account as part of your estimated retirement expenses.

What About Long-Term Care Insurance?

About 1 in 10 Americans older than 65 will spend five years or more in a nursing home, at a potential cost of $50,000 to $100,000 per year.* Because Medicare generally does not cover long-term care, some retirees purchase insurance to cover these potential costs.

Health insurance can be a significant expense.

Long-term care insurance can be complicated and expensive, so be sure to consult with your financial advisor if you are considering such a purchase.

The Impact of Taxes

There is one bill that can decrease for many retirees: the tax bill. Even if you have employment income, your payroll taxes and income taxes may drop significantly.

But other taxes—property taxes, for instance—may increase during retirement. Even income taxes can rise again when you begin taking required minimum distributions from IRAs or other retirement plans.

Your advisor's financial plan will be geared toward minimizing the impact of taxes on your retirement income.

*Source: America's Health Insurance Plans, *Guide to Long-Term Care Insurance*, 2004.

Step 3

Your Income Sources

Most retirees have two main types of income during retirement: regular, ongoing income such as Social Security and pensions; and periodic withdrawals from their investment portfolios. Some also may have income from working part-time or from a trust or other inheritance.

Your advisor can estimate how much you'll need to withdraw from your investments.

We've included a worksheet on page 13 to help you estimate your ongoing income during retirement. If you've gone through Step 2 in this booklet with your advisor, you have a good idea of how much you're probably going to need to maintain the lifestyle you want. Once you provide your sources of ongoing retirement income, your advisor can estimate how much you'll need to withdraw from your investment portfolio each year.

Social Security Income

Although Social Security may account for a relatively small percentage of your retirement income, your advisor will still take it into account. The Social Security Administration mails benefits statements to all workers age 25 and older to provide an idea of what your benefits will be when you retire. Be sure to provide the most recent statements to your advisor.

You can begin collecting benefits at age 62, but if you do, your monthly benefits throughout your retirement can be as much as 30% lower than if you waited until full retirement age. If you want to receive a higher monthly benefit, you may want to wait until your full retirement age or later. However, you must start taking benefits by age 70. Your financial advisor can help you decide the best course of action for your personal circumstances.

Your Full Retirement Age

Birth Year	Full Retirement Age
1937 and before	65
1938	65 and 2 months
1939	65 and 4 months
1940	65 and 6 months
1941	65 and 8 months
1942	65 and 10 months
1943–1954	66
1955	66 and 2 months
1956	66 and 4 months
1957	66 and 6 months
1958	66 and 8 months
1959	66 and 10 months
1960 and after	67

Source: Social Security Administration.

Your Traditional Pension Plan or Cash-Balance Plan

Traditional pension plans and cash-balance plans typically offer several options for taking distributions. Once you provide your financial advisor with information about the distribution options for your plan, he or she can help you make your choice.

Your distribution options may include:

- **Single life annuity.** A fixed amount is paid each month until the retiree dies.
- **Joint and survivor annuity.** A fixed amount is paid each month until the retiree dies. Then a percentage of that benefit is paid each month to the surviving spouse until he or she dies.
- **Term certain annuity.** The retiree specifies monthly payments to continue for a set number of years (usually 5 to 20), even if the pension recipient dies before the end of that period.
- **Lump-sum payment.** The retiree receives a single payment and decides how to invest it. This money is taxable unless it is rolled over to an IRA within a specified period of time.

If you've worked for several employers in your lifetime, be sure to check with all of them to determine what pension benefits you're due in retirement and provide this information to your advisor.

Should You Buy an Income Annuity?

Income (or immediate) annuities are purchased with a one-time, lump-sum payment and provide regular, guaranteed income for a retiree and spouse for life. Your financial advisor can help you decide if an income annuity is right for you.

Other Employer-Sponsored Plans

Your advisor will also need information about your assets and distribution options in other employer-sponsored plans, such as a 401(k) plan or deferred-compensation plan. The distribution options for your 401(k) plan may include:

- **Direct rollover into an IRA.** This allows you to keep your assets tax-deferred and provides the opportunity to invest in a wide variety of mutual funds or individual stocks and bonds.
- **Lump-sum cash payment.** Taking your assets as cash has significant tax implications. Be sure to consult your advisor before exercising this option.
- **Installments.** Some plans allow you to take your assets in monthly or quarterly installments.
- **Leave your money in the plan.** Although your assets remain tax-deferred, this choice limits your investment options to those in the plan.

The distribution options for a deferred-compensation plan can vary widely. Your employer's plan administrator can provide the information your financial advisor will need to help you decide how to manage these assets.

Quick Tip

Some employer-sponsored retirement plans have restrictions on holding stock outside the plan. Consult your plan administrator for information.

Company Stock in Your Retirement Plan?

If you have company stock in your employer-sponsored retirement plan, you generally can either keep the shares or sell them. Your advisor will recommend which approach is best for you and can conduct the transaction when you're ready.

There can be complex tax implications for taking a distribution of company stock, so be sure to consult your advisor about the best way to handle your shares.

Worksheet 1. **Your Projected Retirement Expenses**

Complete the worksheet below to get an idea of your projected expenses during retirement.

Nondiscretionary Expenses	Annual Amount
Mortgage/rent	$
Housing expenses (property taxes, insurance, and maintenance)	
Utilities/telephone	
Transportation (car payments, insurance, fuel, and maintenance)	
Food (groceries and dining out)	
Health insurance premiums (Medicare, Medigap, long-term care, and other health care coverage)	
Other health care expenses (copayments, deductibles, prescriptions, and uninsured expenses)	
Life/disability insurance	
Dependent care (parent or child)	
Clothing	
Cosmetics/toiletries	
Other	

Discretionary Expenses	Annual Amount
Entertainment	$
Hobbies	
Travel/vacation	
Subscriptions/dues	
Gifts/charitable contributions	
Pet care	
Other	

Total Expenses*	**$**

*This figure will be used later to help you evaluate your overall retirement finances.

Worksheet 2. **Your Projected Retirement Income**

Complete the worksheet below to get an idea of your projected retirement income. Then compare your projected income with your projected expenses from Worksheet 1 to determine how much you'll need to draw each year from your investments.

Projected Income			Annual Amount
Social Security	You	$	
	Your Spouse		
Wages	You		
	Your Spouse		
Pensions	You		
	Your Spouse		
Other Income	Rental income		
	Veteran's benefits		
	Other		
Total Before-Tax Income		**$**	

Projected Income Tax Liability — Annual Amount

Estimate the amount of federal, state, and local income taxes on your retirement income. Note that a number of states do not tax certain types of retirement income, including Social Security and pensions. If you are unsure of what rates to use or what assets are taxed, consult your tax advisor.

Federal	$	
State		
Local		

Total Income Tax Liability	**$**	
Total After-Tax Income (subtract income tax liability from before-tax income)	**$**	

Your Annual Retirement Surplus or Shortfall
(subtract your total expenses from Worksheet 1 from your total after-tax income above)

Total after-tax income	$	
— Total expenses (from Worksheet 1)		
Surplus or (Shortfall)	**$**	

Step 4 Your Investment Mix

Once you and your advisor have estimated your retirement expenses and retirement income, you'll probably find that your Social Security benefits and pension aren't enough to meet your expenses, so you'll need to withdraw money from your investment portfolio to cover the difference. Your advisor will then make recommendations for managing your portfolio to provide the greatest possible benefit throughout your retirement years. Here are some things he or she will be considering.

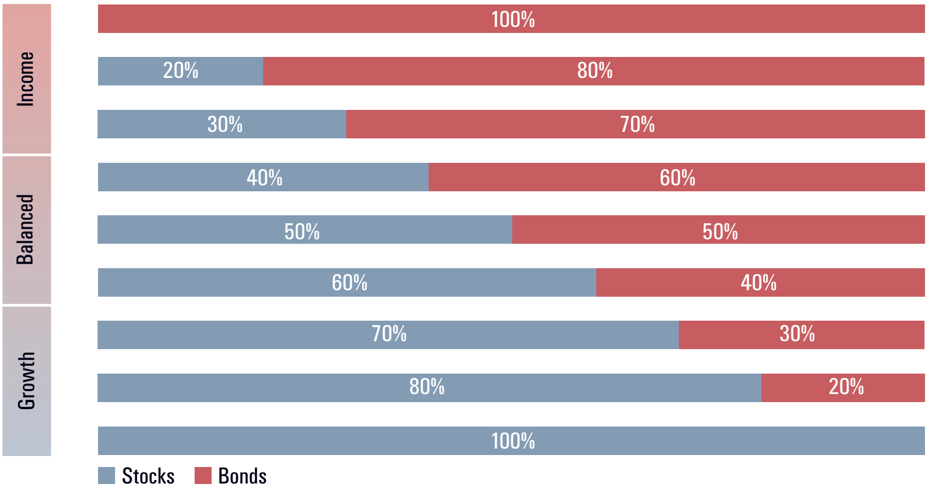
The Right Investment Mix

Chances are good that your advisor will recommend a new investment mix for your retirement years. His or her goal will be to protect your assets from declining in value, while allowing the potential for these assets to grow and keep pace with inflation. Because you may live 30 years or more in retirement, it's usually a good idea to keep at least a portion of your portfolio in stocks for long-term growth. As you move further into retirement, your advisor may recommend changing to a more conservative mix.

Your investment mix depends on several factors, including your investment objectives, time horizon, risk tolerance, and personal situation. Your advisor's goal is to maintain a balanced and diversified portfolio that controls your risk level while providing the right mix of growth, income, and stability.

The chart on this page shows the types of investment mixes that may be considered by your advisor.

Possible Investment Mixes for Retirement



Simplify Your Portfolio

Over the course of your life, you've probably accumulated investments at a number of financial institutions. As your advisor helps you plan for your retirement, he or she may recommend consolidating these assets with a single company.

Consolidation can make it easier and less time-consuming for your advisor to manage your investments and will reduce the number of documents you need for tax purposes. It will also ease the transition if you become incapacitated or die, and your advisor must work with a family member who has been authorized to take charge of your assets.

As part of your asset-consolidation effort, your advisor may suggest that you roll over assets from all your employer-sponsored retirement plans into a single IRA. This can provide your advisor with more control over your investment choices and potentially reduce your costs.

Do You Need to Catch Up?

Don't be surprised if your advisor recommends contributing more to your company's retirement plan and your IRA. If your portfolio took a big hit during the bear market of 2000–2003, or you got off to a late start in saving for retirement, you have a chance to catch up on your savings, thanks to tax law changes that allow you to save more than ever in employer-sponsored retirement plans and IRAs.

Your financial advisor understands that maximizing your savings in these tax-advantaged plans can work to your benefit. However, he or she may also advise you to continue saving the maximum in taxable savings and investments as well, to ensure that you have what you need for your retirement years.

Your Estate Plan

Once your retirement financial plan is in order, your advisor can help you update your estate plan to make sure your assets are properly protected. Your estate plan should include a will that specifies who is to receive your property when you die and who would raise any minor children. You also want to have a living will that provides clear instructions on what your family should do if you become incapacitated and unable to make decisions.

Your advisor will ask you to check the beneficiary designations on your various retirement accounts and life insurance policies. This is especially important because these beneficiary designations override any instructions in your will. Also consider whether you should set up a personal trust to protect your assets. Your advisor can provide a great deal of insight into how to best handle these issues.

Whatever your financial goals, your financial advisor is dedicated to helping you achieve them. It's often been said that retirement is the reward for a lifetime of hard work. Some careful planning during your final years of full-time employment can go a long way toward ensuring that your golden years shine!

Countdown to Retirement

As you can see, there are many factors to consider and decisions to make as you prepare for retirement. Here is a checklist to help you identify the key issues you need to address with your advisor.

Five Years or Less Until Retirement

- ☐ Discuss your retirement plans with your spouse.
- ☐ Prepare a realistic retirement budget.
- ☐ Contact current and former employers for pension and benefits information.
- ☐ Determine what additional health care or long-term care coverage you'll need.
- ☐ Compare your projected income with your projected expenses.
- ☐ Assess the adequacy of your investment portfolio; increase your retirement plan contributions and your savings in taxable accounts, if necessary.
- ☐ Pay off any loans from your employer-sponsored retirement plan.
- ☐ Review your preparations once a year and adjust them as necessary.

One Year or Less Until Retirement

- ☐ Update your retirement budget.
- ☐ Reassess your income sources, including your retirement plan distribution options.
- ☐ Reassess the adequacy of your investment portfolio, and determine if you can still retire in one year.
- ☐ Decide when to retire.
- ☐ Contact your employer's benefits office to begin the necessary paperwork for any retirement benefits.
- ☐ Consider consolidating your assets or rolling over your employer plan money to an IRA when you retire.
- ☐ Make appropriate changes to your asset allocation strategy, if necessary.
- ☐ Obtain any additional health or long-term care insurance that you'll need.
- ☐ Apply for Social Security benefits three months before you want the payments to begin.
- ☐ Sign up for Medicare three months before your 65th birthday. (Note: If you're already collecting Social Security benefits when you turn 65, your Medicare hospital benefits start automatically.)

THE Vanguard GROUP®
Intermediary Services
Valley Forge, PA 19482-2900

For more information about Vanguard® funds, contact your financial advisor to obtain a prospectus. Prospectuses contain more complete information on risks, advisory fees, distribution charges, and other expenses; read and consider them carefully before you invest or send money.

35992-59 012005