

The Road to Retire Well



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Many small decisions...

...Big results



Retirement Plan Basics

- Are you
 - Employed?
 - A business owner?
 - Receiving alimony?
 - Married to someone who works, has a business, or receives alimony?
- Then you can have a tax-advantaged retirement plan.



Retirement Plan Basics

- Defined Benefit Plans
- Defined Contribution Plans



Getting the Most from Employer Plans

- Enroll
- Get the match



Getting the Most from Employer Plans

Example #1: *Matching*

	Max	Julie
Annual salary	\$50,000	\$50,000
% of pay contributed	6%	3%
Employee contribution	\$3000	\$1500
Employer matching	\$1500	\$750
Missed matching \$ (as % of income)	-- --	\$750 (1.5%)



Getting the Most from Employer Plans

- Work long enough to be **vested**.
 - Know your employer's vesting schedule
 - Cliff vesting
 - Graded vesting
 - Immediate for SEP, SIMPLE plans



Getting the Most from Employer Plans

Example #2: *Vesting*

	John	Linda
Length of employment	2 yrs, 11 months	3 years
% of pay contributed	6%	6%
Employee contribution	\$3000 per year \$8750 total	\$3000 per year \$9000 total
Employer matching	\$1500 per year \$4375 total	\$1500 per year \$4500 total
Vested matching	0%	100%
Total retirement savings	\$8750	\$13,500



Getting the Most from Employer Plans

Defined Benefit Plans

- Know the plan's formula; make it work for you.
- Factors
 - (High) (Final) Average salary
 - Years of service
 - % per year of service



Getting the Most from Employer Plans

Example #3: Defined Benefit Plans

Factors

- Salary: Average final 5 years
- Years of service
- 2% per year of service
- 6% reduction for each year < age 60



Getting the Most from Employer Plans:

Example #3 (part 1): **Defined Benefit Plans**

	Rachel	Jack
Years service	10 years	15 years
Salary		
Final year	\$50,000 *	\$53,000
-1	\$44,000	\$51,560
-2	\$43,200	\$51,500
-3	\$42,700	\$50,900
-4	\$42,000	\$50,000 *



Getting the Most from Employer Plans

Example #3 (part 2): **Defined Benefit Plans**

24	Rachel	Jack
Final average salary	\$44,380	\$51,560
Normal annual benefit	\$8,876	\$15,468
Reduction: Early retirement	18%	--
Actual benefit	\$7278 just 47% of Jack's	\$15,468



Make Use of IRAs

Anyone with

- Earned income
- Alimony
- A spouse with earned income or alimony

can contribute to some type of IRA.



Make Use of IRAs

Consider an IRA if:

- No employer plan.
- Not working, but spouse is.
- Employer plan maxed out.
- Employer plan has high expenses or poor investment choices.
- Want Roth but not offered by employer.
- Self-employed but no plan set up.
- Need April 15 grace period.



Make Use of IRAs

- Set up IRA at almost any financial institution.
- Purchase almost any type of investment.
- Contribution limit: the annual limit or the amount you earned, whichever is less:
 - \$5000
 - Indexed in future years.
 - \$1000 catch-up contribution for ages 50 and older.



Make Use of IRAs: Options

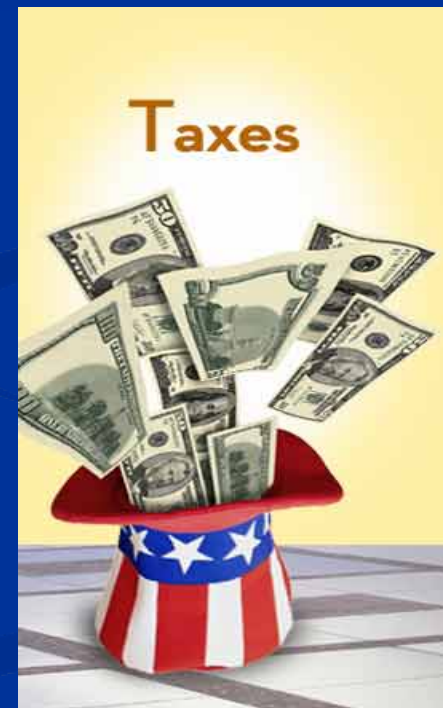
- Roth IRA
 - Income limits
- Deductible contributions, traditional IRA
 - Income limits if have employer plan, or spouse does
- Non-deductible contributions, traditional IRA



Tax Benefits

Traditional vs Roth

- Tax deferral: Traditional versions
 - IRA
 - Most employer plans
- Tax-free: Roth versions
 - Roth IRA
 - Roth 401(k)
 - Roth 403(b)



Tax Benefits:

Tax Deferral

Advantages:

- Reduces current income taxes.
- No taxes until withdrawal.
- Pay taxes at a lower rate in retirement.
- Pay tax with dollars that are worth less.



Tax Benefits:

Tax Deferral

Advantages (cont.):

- More likely eligible for income-tested tax breaks and benefits.
- Illinois residents only: Distributions from employer plans are not subject to state income tax.



Tax Benefits:

Tax Deferral

Disadvantages:

- Tax rates might go up.
- Regular tax rates apply, rather than lower capital gains rates.
- Heirs owe income taxes on distributions.
- Early withdrawal penalties.



Tax Benefits:

Tax Free

Advantages:

- Tax-free distributions on all future growth.
- Hedge against future tax rate uncertainty.
- Heirs also receive tax-free.
- Take advantage of lower income years.



Tax Benefits:

Tax Free

Advantages (cont'd.)

- Reduce taxes on Social Security retirement benefits; qualify for other income-tested benefits.
- Retirement income flexibility without tax consequences.



Tax Benefits:

Tax Free

Advantages: Roth IRAs only

- Access to contributions before age 59 1/2 without tax or penalty.
- No required minimum distributions for account owner
 - There are RMDs for beneficiaries.



Tax Benefits:

Tax Free

Disadvantages

- Pay taxes now.
- May be in lower tax bracket in retirement.
- Loss of eligibility for other tax breaks due to increased income



Maximize Tax Benefits

- When you change jobs, preserve the tax benefits of your retirement plan \$:
 - Rollover to an IRA.
 - Transfer to new employer plan.
 - Leave with old employer.



Don't take the money out and spend it.



Maximize Tax Benefits

Example #4: Rollover

Co-workers Linda & Miguel:

- 100% vested (3 years)
- Contributed 6% (\$3000 per year)
- Received 3% match. (\$1500/yr)
- Total in account: \$13,500



Maximize Tax Benefits

Example #4: Rollover

	Linda	Miguel
Total in account	\$13,500	\$13,500
Decision	Take out	Rollover to IRA
Income taxes (25% + 3%)	\$3780	\$0
Penalties	\$1350	\$0
Balance	\$8370	\$13,500



Maximize Tax Benefits

- Contribute the maximum.
- If you're 50 or over, use the catch-up provision to contribute more.
- Claim the Saver's Credit.
- Set up an IRA for a non-working spouse.
- Keep the money in a plan until age 59½.
- Get professional advice, esp. if you have company stock in your account.



What about Annuities?

- Sold as investments with tax benefits and guarantees.
But:
 - Commissions.
 - High annual fees.
 - Surrender fees.
 - Some have risk if insurance company insolvent.
- Employer plans & IRAs have much better tax benefits.
- Max out employer plans and IRAs first.
- Get advice if considering an annuity.



Government Workers

- If government earnings were not subject to Social Security, Soc Sec may reduce benefits based on government pension.
 - Government Pension Offset
 - Your Soc Sec benefit as a spouse or widow may be reduced.
 - Windfall Elimination Provision
 - Soc Sec benefits earned on your own work record may be reduced.



Government Workers

- Would additional years in Social Security earn you a benefit, or increase it?
- Use online calculator at www.ssa.gov or download.
- Talk to Social Security representative before making decisions.



Get Help If You Need It

- Employer plan questions?
 - HR or plan provider
- Investing?
 - Look for free or lost-cost help from:
 - Plan provider.
 - Mutual fund where you invest.
 - www.RetireWell.uiuc.edu



Get Help If You Need It

- Financial planning: Look for fee-only advisers.
 - www.NAPFA.org or 888-FEE-ONLY
 - www.GarrettPlanningNetwork.com
- Extension lesson, *Choosing a Financial Professional*.



Action Steps

Put yourself on the road to retire well.

- Learn more about employer's plan.
- Sign up & start saving.
- Increase the amount I'm saving.
- Plan for job changes or retirement.
- Get help if I need it.
- Other



Additional Resources from U of I Extension

- *Rules for Taking Distributions from Tax-Deferred Retirement Plans*
<http://www.ace.uiuc.edu/cfe/retirement/takingdistributions2007.PDF>
- *Plan Well, Retire Well* www.RetireWell.uiuc.edu
 - How much do I need to save for retirement?
- *Is Your Financial Security at Risk?*
www.urbanext.uiuc.edu/Risk?
- *Your Retirement Checklist* (\$19.99) 800-345-6087
- *IRA Basics* <http://www.ace.uiuc.edu/cfe/retirement/>



Plan Well, Retire Well: Your How-To Guide

Plan Well,
Retire Well

www.RetireWell.uiuc.edu



The Road to Retire Well

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Disclaimer:

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