

RETIREMENT: The Vacation You Never Dared to Dream of
By Elaine Kiernan

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Many of us, after spending time researching the retirement process, are surprised to find out just how much needs to be saved. Between new legislation, modifications in IRS regulations, and the uncertain future of Social Security System, protecting our well-being when we decide to stop working can be a daunting task. The fact is, most aren't doing nearly enough. It is never too early to set aside funds for retirement, and the ones who find themselves in the best retirement positions are the ones who decided to have a *disciplined* savings program in place—periodic or haphazard saving becomes counterproductive.

In today's market, fewer employees enjoy employer-sponsored pension and retirement plans when compared to the dot-com 1990s. It is increasingly common for *employees* to take the full responsibility for funding their retirement through defined contribution plans like 401(k)s, ROTHs, and IRAs. Many investors—without a guaranteed pension and unaware of alternatives— are left uncertain and worried about how to amass and invest their earnings to ensure a comfortable retirement.

The first step in your retirement plan should be to estimate an appropriate cost of living in retirement. This way, by working backwards, you can set target goals and structure a savings plan that will keep you living comfortably. Many suggest an estimate of 70% of your current income, but I recommend aiming for 100%. This will keep you prepared for unpleasant surprises and allow you to replace work-related expenses with leisure and travel expenses that you will no doubt desire. Consider small deductions from each paycheck sent to a retirement account like a 401(k).

For those eligible for federal or state pensions and are planning to use them to buffer Social Security benefits, know that the amounts are combined: you cannot receive the full amount from both. You do have options. Pensions can be offered in:

- A. A full unmodified amount
- B. Optional modified amounts
- C. Smaller installments
 - Allows your spouse to continue receiving your pension after your death
 - If your spouse dies first, you will be limited to the modified smaller amounts
 - If you remarry, your new spouse cannot qualify for the continued benefits after your death

I recommend *pension maximization* by choosing the full unmodified amount and then using the difference between that amount and the hypothetical modified amount to purchase life insurance. This strategy allows your spouse to receive the insurance benefit instead of your pension should you pass away first. In the case where your spouse dies first, you continue to receive your full unmodified pension benefit.

If ineligible for pension, consider a 401(k) pretax retirement savings program sponsored by your employer (which is sometimes matched by them under a plan called a vesting schedule). Five-year vesting schedules—where 20% of the amount contributed is vested after one year, 40% after two years, 60% after three years and so on with 100% vesting after five years of service—are most common (you are always 100% invested in your *own* contributions). If you resign, you can either roll the pension to a 401(k) with your new employer or transfer it to an IRA account. When you retire, any loan on your 401(k) will automatically be considered a premature withdrawal with a 10% penalty plus taxes.

IRAs (Individual Retirement Accounts) are another form of employer-sponsored retirement plans. Employers traditionally contribute 1% of your salary the first year, 2% the second year and so on, regardless of whether or not you contribute to it. You can contribute \$3,000 (year 2003)¹ per person. There is also a new IRA plan called ROTH IRA that has some key differences with traditional IRAs:

IRAs

- Money grows tax deferred
- Cannot be withdrawn until age 59
- You are required to begin minimum withdrawals by age 70 to avoid a penalty
- Under IRS code 72T, withdrawal of funds prior to age 59 is allowed only if it is in equal and periodic installments continuing for a minimum of five years or until you reach age 59.*

vs.

Roth IRA

- Money grows *tax free* instead of *tax deferred*
- Withdrawals are also *tax free*
- You do not have to wait till age 59 to make a withdrawal
- After a minimum of five years, up to \$10,000 can be withdrawn for a first time home purchase
- You can leave all the funds to your beneficiary without making any withdrawals.

Year 2004-2005	\$3,500/person/year
Year 2006	\$4,000/person/year
Year 2007	\$5,000/person/year

¹ See IRS Publication 590-03, "Individual Retirement Accounts (IRAs)", for more information.

*[*The amount you are allowed to withdraw is based on current age and estimated mortality age. It's a good idea to consult your financial planner to obtain an estimate]*

A third popular option is an employer-sponsored profit sharing plan. If you are self-employed, you can set it up for yourself, and it doesn't require a mandatory contribution. You can elect to contribute up to \$40,000/year tax deferred. If there are employees in the company, then the employer must contribute the same percentage on their salary as the employees do.

Once you ARE retired, we recommend not relocating for at least a year: Consider getting acclimated to retired life before making any major changes. Many consider relocation for warmer climates, a lower cost of living, or for proximity to grandchildren or family. If you plan a sensible realistic budget, you can look forward to a delightful retirement spent fulfilling the dreams you had put on hold.

About Elaine Kiernan:

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She is President of Financial Resource Associates, Inc. (www.FRAssociates.com), a Registered Principal/Branch Manager of Geneos Wealth Management, Inc. and holds memberships in the Financial Planning Associates (FPA)- 2007 co-President, Monterey Chapter, the Institute of Divorce Financial Analysts (IDFA), and the International Association of Collaborative Professionals (IACP). Her firm, Financial Resource Associates, Inc. is a Registered Investment Advisory firm and she has reached her 25th year in practice in 2007. She is licensed by the California Department of Corporations, and the NASD.

Elaine and her firm specialize in all aspects of financial planning, divorce services, small business services, same-sex issues, insurance, and retirement.

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