volume 7, number 5

21st century retirement

Dan Gaugert, CLU, ChFC

525 E. Jones St.
Raleigh, NC 27601-1137
V: (919) 863-4111
F: (919) 836-8045
dan@gaugertfinancial.com
gaugertfinancial.com

Securities Offered through Capital Investment Group, Inc. 17 Glenwood Ave. Raleigh, NC 27603 919-831-2370 Member NASD/SIPC

in this issue:

Should Retirement Be Hard Work?

Living Longer—It's Part of the Equation Too

The "What" and "Why" Behind Estate Planning

What Is a 403(b) Plan?

Planning IRA Distributions

In 2002, the Internal Revenue Service (IRS) finalized rule changes that make it much easier for taxpayers to determine how much they must take out of their retirement plans or traditional *Individual Retirement Accounts (IRAs)*. In fact, taxpayers can now choose to keep money in their plans or IRAs *longer*, where it may continue to grow on a tax-deferred basis.

For years, the *required minimum distribution (RMD)* rules have forced taxpayers to make critical decisions—once they retired or reached age 70½—regarding who their *beneficiaries* would be and how they would calculate their annual distributions. Under these rules, individuals must start withdrawing money from their plans or IRAs by the *required beginning date (RBD)*, in most cases, April 1st of the year after the year in which they reach age 70½. However, they can always take out *more* than the minimum required. (*Note*: The minimum distribution rules do not apply to *Roth IRAs* while the owner is alive.)

This has been an important issue for many taxpayers, but especially for more affluent individuals who are able to maintain a comfortable retirement lifestyle from other sources, and who want to save their plans or IRA assets in a tax-deferred vehicle for as long as possible. This is because assets left in a plan or IRA can serve as a cushion for the retiree and also as a legacy to pass on to heirs. For these taxpayers, the goal is to take out only the *minimum* amount required.

Lifetime Distributions

Calculation Changes. Minimum distributions are now calculated according to one standard table (***uniform life expectancy***) based on the joint life expectancy of the taxpayer and a hypothetical beneficiary who is ten years younger, even if no beneficiary is named. There is an exception that applies when the designated beneficiary is a spouse who is *more* than ten years younger than the owner. In that case, a separate, generally more favorable table (***joint life and last survivor***) is used. The bottom line—simpler calculations and smaller required distributions for most people.

continued on page four

Should Retirement Be Hard Work?

Retirement *should* be a time to relax free from financial worry. Many people dream of retirement as a time to travel, or a time to pursue hobbies or special interests—a break from a 40-hour workweek. But without careful retirement planning, you may actually face the prospect of working harder and longer during your so-called retirement years than you ever imagined. With this in mind, it may be safe to say that the best-laid plans begin well before the age of 65.

Know Your Resources

How many times have you said "I'll do that when I retire," expecting to have more time to pursue other interests when you no longer have to report to the office every day? But, have you considered what may be the costs of these interests? A general rule of thumb is that you will need 60%–80% of your pre-retirement income to maintain your lifestyle during retirement. Careful planning can help offer security and comfort in retirement, along with the resources to pursue these new interests.

For many, Social Security, employer-sponsored retirement plans, and personal savings are the primary sources of retirement income. Although Social Security may contribute a certain percentage, the Social Security Administration (SSA) estimates that for the average worker, benefits replace only 40% of pre-retirement income (SSA, 2002). Although, for many, an employer-sponsored retirement plan can also contribute substantially. However, both of these sources may need to be supplemented with personal savings to help provide enough income to maintain the lifestyle to which you may have become accustomed, and/or even provide the extras you look forward to in your retirement years.

Put Time on Your Side

Early retirement planning puts time on your side. It is never too early to begin saving and never too late to start. In fact, one advantage to early retirement planning is that the longer you have before retirement, the greater your opportunity to increase your savings through potential growth.

An equally important consideration for retirement planning is the ever present reality of inflation, which can quickly shrink even a substantial savings total. For example, a modest 4% inflation rate, maintained over 15 years, will reduce the purchasing power of $250,000 to $138,816. Starting early may help your savings outpace inflation.

Although it can be difficult to imagine a time when you will not have to be at the office or worksite in the morning, the day will be upon you sooner than you think. With this in mind, planning for retirement *now*—even if it seems premature—may help ensure a secure financial future for you and your family.

Living Longer—It's Part of the Equation Too

One interesting factor changing the shape of retirement planning is the steady increase of life expectancies for Americans. Given this population trend, many people may spend one-third of their lives in retirement. Relying on retirement plans and Social Security will be increasingly difficult because these programs were not initially designed to provide *perpetual* income. Thus, your retirement assets, as well as your personal savings, will have to work longer and harder to help fulfill your personal objectives, regardless of whether or not you retire early.

Life Expectancy of All Americans—1940–2003*

Year	Male	Female	Both Sexes
2003	74.8	80.1	77.6
2000	74.1	79.5	76.9
1990	71.8	78.8	75.4
1980	70.0	77.4	73.7
1970	67.1	74.7	70.8
1960	66.6	73.1	69.7
1950	65.6	71.1	68.2
1940	60.8	65.2	62.9

*Life expectancy at birth for all races.
Source: *National Center for Health Statistics, 2005.*

The "What" and "Why" Behind Estate Planning

Many individuals put off planning their estates. For some, this is due to the misconception that estate planning is only necessary for the wealthy or only involves tax planning, which can be done "later." For others, it's because they simply have a difficult time contemplating their own death—a perfectly natural reaction. Yet, it is important to recognize that regardless of these issues, *solidifying the future of your family* is probably high on your list of priorities. That's why a well-structured estate plan is invaluable. Through it, you can control the distribution of your assets and possessions during your lifetime and after your death, as well as name guardians for your children or plan care for other dependents.

Getting Started

Individuals involved in the estate planning process should work with an estate planning team, including their own personal legal or tax counsel. For some, this initial step is a difficult one, because it requires sharing personal thoughts, fears, wishes, and financial affairs with others. Your attorney will play an instrumental role in preparing any necessary legal documents. However, your financial professional, bank trust officer, insurance professional, or accountant may also need to become involved. Generally, the size and complexity of your estate, as well as the existence of an established relationship with an advisor, will dictate the overall involvement and/or need for additional professional expertise or emotional support.

Initially, your estate planning team will focus on your current financial position. This is a very important part of the estate planning process, because you need to know where you stand *today* in order to accurately plan for the *future*. For this reason, you will need to gather any and all materials involving current or future income, property ownership, insurance, and legal arrangements already in place. This may require you to divulge a lot of private information, but it is a necessary part of the estate planning process. Here is some of the information you'll need to provide:

- Current income from employment and all investments.
- Investment documents, certificates, statements, passbooks, etc.
- All retirement benefits: Social Security (including survivors' benefits), Individual Retirement Accounts (IRAs), pension and profit-sharing plans.
- Any expected deferred compensation.
- Deeds to primary and vacation residences.
- Life insurance policies of which you are the owner, the insured, or the beneficiary.
- A list of all personal property.
- Current and expected debts and obligations, including mortgage and loan balances, real estate liens, taxes payable, consumer debts, and estimates of funeral costs and estate settlement expenses.
- Your will, if you have one.
- Trust agreements, if any.

A complete analysis can begin once you've assembled this information. This will allow you to take a closer look at your family's needs. Some important questions that you will find answers to are:

- How will your family's overall cost-of-living requirements change in the years ahead?
- Who will take care of any minor children if something happens to you?
- Who will make medical and financial decisions on your behalf if you become incapacitated due to illness or injury?
- What are the estimated educational expenses when your children reach college age?
- Is there a family member who needs special care or medical attention?
- How will estate taxes affect your assets as they are currently held?

Keep an Open Mind

The careful planning of an estate requires you to share a lot of personal and financial information with one or more professional advisors. This fact alone often serves as an initial stumbling block to the planning process. However, bear in mind that with an accurate financial and personal portrait, it will be easier to tailor your estate plan to accomplish your specific goals and objectives. In addition, while most of your initial time will be spent creating your first estate plan, your circumstances—both personal and financial—are bound to change over time. Therefore, your estate plan will need to evolve so it will continue to address your needs and wishes.

By keeping an open mind and placing your trust in a competent advisory team, you can help ensure that your wishes for asset control and distribution will fall nothing short of your expectations.

planning IRA distributions

continued from page one

Post-Death Distributions

Simpler Rules. The old rules had many separate provisions, depending on whether the taxpayer died before or after the RBD. The revised rules simplify things by applying a single rule regardless of when death occurs—that is, the designated beneficiary may take payments over the beneficiary's remaining life expectancy.

Changed "Default" for Distributing Remaining Assets. Under the old rules, if the taxpayer's death occurred before his or her RBD, the plan or IRA account balance had to be distributed by the end of the year containing the fifth anniversary of the taxpayer's death. If beneficiaries wished to instead take distributions over their life expectancies, they were required to make that election no later than December 31st of the calendar year after the taxpayer's death. With the changes, the default is now a life expectancy option in which distributions *start* by December 31st of the calendar year after the taxpayer's death. Of course, they can always withdraw more assets if needed.

Designating Beneficiaries

Under the old rules, the determination of designated beneficiaries occurred upon the RBD (or date of death, if earlier). Now, the designated beneficiary may be determined on September 30th of the calendar year following the year of the taxpayer's death. This later deadline leaves open many estate planning opportunities for the taxpayer, even after RMDs have begun, and can help simplify post-mortem planning for the beneficiaries.

These simplified rules should make planning easier for retirees and their beneficiaries. In addition, taxpayers who wish to preserve more of their assets in an IRA for a longer period of time now have the opportunity to do so.

What Is a 403(b) Plan?

In 1958, the Internal Revenue Service (IRS) created *403(b) plans* to encourage employees of certain organizations to begin saving for retirement. Organizations eligible for participation in these plans are those "organized and operated exclusively for religious, charitable, scientific, public-safety testing, literary, or educational purposes."

Although employees of qualifying organizations may be entitled to receive a pension at retirement, many find that pension proceeds are not as high as pre-retirement income. Contributions to a 403(b) plan can be a significant supplement to pension proceeds. Furthermore, 403(b) contributions are taken from gross pay and are made with pre-tax dollars, which can often mean that there is not a significant reduction in net pay. All funds in a 403(b) plan grow tax-deferred, and earnings accumulate without taxation until withdrawal. Withdrawals made before the age of 59½ may be subject to a 10% federal income tax penalty.

The information provided is not written or intended as tax or legal advice and may not be relied on for purposes of avoiding any Federal tax penalties. Individuals involved in the estate planning process should work with an estate planning team, including their own personal legal or tax counsel.

21st Century Retirement is published for the Society of Financial Service Professionals by Liberty Publishing to help keep you up-to-date on the issues which may affect your financial well-being. The opinions voiced in this material are for general information only and are not intended to provide specific advice or recommendations for any individual. For specific advice on how to apply this information to your particular circumstances, you should contact your insurance, legal, tax, or financial professional. Printed in September 2005.
Copyright © 2005, Liberty Publishing