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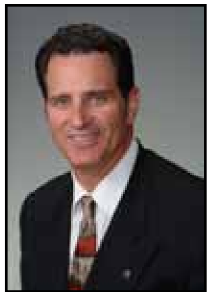
21st century retirement



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Keep Your Retirement Savings on Track during Career Transitions

Nowadays, individuals change jobs many times throughout their working lives. If you are starting a new phase in your career, you are probably considering how you will handle your finances while making the transition. One important aspect is your retirement plan funds. If you have accumulated savings in a 401(k), 403(b), or similar employer-sponsored retirement account, you need to decide how to manage those funds upon leaving your current position.

Generally, you have the choice of transferring, or cashing in, or reinvesting your retirement plan savings. The choice you make may depend on both your short- and long-term goals. Let's explore the options.

A simple way to consolidate your savings is to transfer funds from your previous employer's retirement plan into your new company's plan. You may also choose to leave your money in your former employer's plan, but depending on the terms, you could be subject to service fees or limited contribution and distribution options. If, however, you have an outstanding loan from your previous employer's plan, or if you stand to lose certain retiree benefits by exiting completely, you may want to remain invested for a period of time after leaving your job.

Taking a cash distribution is another option, but consider the ways this may negatively affect your retirement strategies. Besides owing potentially significant income tax on pre-tax contributions, you may be subject to a 10% penalty if you are under the age of 59½. In addition, you may forfeit the long-term benefits associated with tax-deferred earnings, potentially making it more difficult for you to accumulate the resources you need in retirement.

To keep your retirement savings on track and avoid an immediate tax bite, consider rolling your 401(k) assets into an Individual Retirement Account (IRA). There are two ways to roll over funds:

1) With the first method, known as an indirect rollover, your former employer makes the distribution payable to you, less 20%, which is withheld in Federal taxes. You must then reinvest the distribution into an IRA or other qualified plan within 60 days. In order to achieve a tax-free rollover with this method, you must reinvest the full distribution amount, which

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Give Your Kids a Head Start with a Roth IRA

It may be difficult to convince your teenagers to participate in their financial futures, but if you can persuade them to contribute at least part of their babysitting or after-school job money to a Roth Individual Retirement Account (IRA), they may thank you later.

Although it is a retirement account, anyone with earned income below $122,000 for single filers and $179,000 for joint filers in 2011 can open a Roth IRA. Contributions are nondeductible, but earnings and qualifying distributions accumulate tax free. Because children seldom make enough to owe income tax, they are usually better off with a Roth IRA than a tax-deferred traditional IRA. For 2011, your child can contribute $5,000 (or earned income, whichever is less) to a Roth IRA.

Saving for retirement early can generate substantial results. Suppose your 14-year-old daughter uses $1,000 to open a Roth IRA. If she makes no additional contributions and the funds grow at 8% annually, she will have more than $50,000 to withdraw tax free at age 65. Or suppose your son opens a Roth IRA with $2,000 when he is 15-years-old, and then he contributes $2,000 annually for the next 10 years. The estimated value of his tax-free fund balance at age 65 will exceed $700,000, if the annual growth rate is 8%.*

A Roth IRA offers the greatest growth potential if the account is left untouched until the holder reaches the age of 59½. At that age, the holder can withdraw earnings tax free, provided he or she has owned the account for five years. The IRS does permit penalty-free early withdrawals to pay for education or to help with a first-time home purchase. However, taxes will be owed on nonqualified early withdrawals.

Before you open a Roth IRA for your child, bear in mind that you cannot stop your child from withdrawing money from the account whenever he or she wants after reaching the age of majority, which is 18 in most states. If you are uncertain about your child's ability to handle money, opening an account in his or her name may not be the best choice.

Also, be aware that only taxable compensation income can be contributed tax free to a Roth IRA. In general, paying your children for doing chores around the house does not qualify as compensation income, as this is an intrafamily transaction not usually reported to the IRS. However, if you own your own business, you are permitted to hire your minor children to do certain jobs. Provided you pay your children a fair market wage for the services performed, their earnings would be considered compensation income and could be invested in a Roth IRA.

It is essential to keep detailed records of how the money placed in a Roth IRA was earned, even if a teenager's working arrangements were informal (e.g., babysitting or mowing lawns for neighbors) and he or she did not earn enough to owe income tax. Penalties could apply if the IRS determines the funds contributed to a Roth IRA were not compensation income.

The good news is that, if your teenager goes out and blows his paycheck on a new cell phone and skateboard, all is not lost. If, for example, your son earned $2,500 over the summer but spent all the money, you could still contribute the amount equivalent to his taxable earnings into a Roth IRA on his behalf, thereby helping to ensure he has something set aside when he retires and his skateboarding days are behind him. ■

**The hypothetical examples are for illustrative purposes only. They are not intended to reflect an actual security's performance. Investments involve risk and may result in a profit or a loss. Seeking higher rates of return involves higher risks.*

Social Security and Retirement: What You Need to Know

When contemplating retirement, you may be counting on Social Security benefits to provide you with a basic level of income. However, the *age* at which you choose to retire is an important part of the equation. There are also other issues to consider when making your retirement decisions.

Ask yourself the following questions: 1) How would an early retirement, for example at age 62 versus age 65, affect your Social Security benefits? 2) How will those benefits be taxed? 3) Is it in your best interest to continue working to earn extra income when your Social Security benefits could be reduced, based on your earnings?

What's the Maximum?

Social Security provides only a base level of income. The maximum benefit for a person who retires in 2011 at **full retirement age** is $2,366 per month. In 2010, the maximum benefit was $2,346 per month. It is important to note that the benefit for a non-working spouse is 50% of that amount.

Should You Delay Retirement?

If you delay retirement past your full retirement age, your monthly benefit will increase, based on the age at which you elect to take retirement benefits. But when you reach age 70, the benefit increase no longer applies, even if you continue to delay the payment of benefits.

Taking benefits at age 62, which is considered early retirement, is appealing to many people. However, if you decide to take early retirement benefits from Social Security, your monthly benefit amount will be permanently reduced by 20–30%, based on your full retirement age.

Some people continue working and earning additional money to supplement basic Social Security income. This is where you need to be careful. If you earn more than the maximum amount allowed, you may forfeit some of your benefits. If you are under full retirement age, receive Social Security benefits, and earn additional income, your benefits will be reduced by $1 for each $2 you earn over $14,160 in 2011. During the year in which you attain full retirement age, your benefits will be reduced by $1 for every $3 earned over a certain amount ($37,680 in 2011). Upon attainment of full retirement age, there is no earnings limit, and Social Security benefits will not be reduced.

Full Retirement Age Is Changing

For a long time, full retirement age was 65. Due to longer life expectancies, that age is increasing gradually until it reaches age 67. This change began in the year 2000 and affects people born in 1938 and later. Age 62 remains the earliest you may begin to receive Social Security retirement benefits.

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includes the 80% you receive in cash, as well as 20% from your own funds to account for the amount withheld. Your withheld funds will be refunded after you file your tax return, provided your rollover occurred within the 60-day time limit. Failure to reinvest the 20% withheld will result in income tax and a 10% Federal income tax penalty if you are under the age of 59½.

2) To avoid the 20% withholding requirement, you may request a direct trustee-to-trustee transfer to an IRA set up in your name or another qualified plan. Be aware that not all qualified plans accept this type of transfer. Because this method is considered a distribution option, spousal consent and other similar participant and beneficiary rules of protection may apply.

There are many factors to consider when deciding how to manage your retirement plan funds during a career transition. Bear in mind that your decisions in the short-term can have an impact on your long-term plans. For specific guidance, be sure to consult your financial and tax professionals. ■

Retirement Planning: Key Factors to Consider

Even if your retirement seems a long way off, you can help prepare for the future and think about what you can do *today* to help ensure a secure retirement *tomorrow*. Although time may be on your side, if you ask some of the retirees you know, they may tell you that saving for retirement is not as simple as it initially appears.

Here are four key factors to consider when planning for your retirement:

1) Inflation. You may be aware that, over time, inflation can erode your savings. But, many people don't realize the potentially serious effects of inflation. At 3% inflation, $100 today will be worth only $67.30 in 20 years—a loss of one-third of its value. At 35 years, this amount would be further reduced to just $34.44. Thus, it is important to seek retirement savings vehicles that have the best chance of outpacing inflation.

2) Taxes. Your present income level, tax bracket, and the types of tax-deferred retirement savings plans that are available can all play an integral part in how much money you can save for your retirement. By maximizing your pre-tax contributions to employer-sponsored plans and **Individual Retirement Accounts (IRAs)**, you can take advantage of the tax-deferred benefits of such plans.

3) Compound Interest. Becoming a disciplined saver is one of the key components of retirement plan success. By making regular contributions to your employer-sponsored retirement plan and your IRA, you can maximize the power of **compound interest** (the interest earned not only on the initial principal, but also on the accumulated interest from prior periods). With consistent contributions, your retirement savings have a greater chance of accumulating to meet your long-term goals.

4) Personal Savings. Considering the effects of inflation, it is possible that your retirement plan income may fall short of your needs, especially during a long retirement. Furthermore, Social Security generally provides only a base level of retirement income. So, to avoid a potential shortfall, start planning to supplement your retirement income with personal savings.

While understanding these principles is no guarantee of future success, they can get you started on the right path. The sooner you recognize the effects that economic forces can have on your retirement income, the more likely you may be to adopt strategies that can help you achieve your long-term objectives. Being proactive today can help increase your retirement savings for tomorrow. ■

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For Your Information

The Social Security Administration (SSA) provides a free service that allows you to check the accuracy of your Social Security records. To learn more, call Social Security at 800-772-1213 or visit www.ssa.gov to request a *Social Security Statement* (Form SSA-7004). Once you complete the request, you'll receive an annual breakdown of salary credited to you since 1950, as well as an estimate of benefits you will receive upon retirement. ■

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