

21st century retirement



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Americans are living longer, healthier lives than ever before. As a result, for many people, retirement may last 20 years or more. So, if “time is money,” how many years do you have in the bank? Because inflation will most likely decrease the purchasing power of your money over time, your dollars may buy less during your retirement than they do today. For example, at 3.5% inflation, \$100 today would be worth only \$42.31 in 25 years, and this amount would be further reduced to \$30.00 in 35 years.

The sooner you start building your nest egg, the longer it has to grow. Consider the following examples that assume no taxes or inflation. Suppose, at age 25, you save \$100 per month for 20 years and earn 6% interest. If you make no additional contributions after the age of 45 and your savings continue to earn 6% interest, at age 65 your savings will be worth \$148,182. However, if you don’t begin until age 45 (saving \$100 per month for 20 years at 6% interest), at age 65 your savings will be worth *only* \$46,204. In order to achieve savings of \$148,182 over 20 years, you would need to earn interest at a rate of approximately 15% per year—or save significantly more than \$100 per month!

While both scenarios illustrate the same amount of money being saved per month, the additional 20 years and the **compound interest** factor make a big difference. If you are in your prime earning years and start setting money aside *now*, you may have a better chance of meeting your retirement funding goals.

Identify Your Goals

The first step in preparing for your retirement is to determine your objectives. How do you envision your “golden years”? Spend some time thinking about what is really important to you, and consider what you want your future to look like. For example, at what age do you want to retire? Where do you see yourself living? Do you expect to travel frequently? Would you like to continue to work on a part-time basis? Do you see yourself playing golf every day? These questions and others can help you shape a vision for your retirement.

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A New Ball Game for Early Retirees

An early retirement is on everyone's "wish list." A relaxing lifestyle in a warmer climate or the pursuit of a hobby typically characterizes the vision of a comfortable retirement. Today, however, it's a new ball game. Unfortunately, retiring *later* than anticipated is becoming a fact of life. On the other hand, there are some issues you can address in advance that may help you defy the increasing norm.

The key is to take a *proactive* role when planning your retirement, especially if you wish to retire early. Today, it is not uncommon for some retirees to require between 60% and 80% of their pre-retirement income in order to meet expense and income needs consistent with their desired standard of living. Naturally, the *sooner* you begin planning, the better your chances for early retirement. However, it is equally important to note that most people who have managed to retire early have recognized the changing concept of retirement.

Various factors are redefining how Americans approach retirement. Due to financial necessity,

or sometimes an overabundance of leisure time, some retirees are beginning to return to the workplace. For example, many retired executives are starting their own part-time consulting businesses. Part-time work during retirement may be worth consideration as a part of your overall financial plan.

Another interesting factor that is redefining retirement is that life expectancies continue to increase over time. For some, spending one-third of their lives in retirement is a possibility. Relying on qualified retirement plans and Social Security may not be sufficient to fund your retirement. Adding to the dilemma of increased longevity, qualified retirement plans have gradually shifted the savings responsibility from employers to employees. Thus, your retirement assets, as well as personal savings, are in your hands, and they will have to work longer and harder to help fulfill your objectives, regardless of whether you retire early or not.

An often overlooked aspect of retirement planning is money

management once retirement has begun. To ensure that you have adequate retirement assets, your money may have to continue working for you throughout your retirement years. In addition, inflation—along with the amount of withdrawals from your qualified plans and other assets—will have a direct impact on the longevity of your retirement assets.

It is also important to note that early retirement may incur certain tax penalties on early withdrawals from retirement plans. All options need to be investigated. Before taking action, consult your professional tax, legal, and financial advisors to determine the overall impact on your long-term financial goals.

For many people, financial planning and part-time work have become essential components of a comfortable retirement. By maximizing your personal savings, you will increase your chances of reaching your retirement goals, which is particularly important if you are contemplating early retirement. ■

Baby Boomers and the Changing World of Retirement

Over the next two decades, the most chronicled generation in the United States will gradually enter retirement. At that point, each wave of Baby Boomers will learn if their retirement plans, Social Security, and personal savings are sufficient to maintain their existing lifestyles and meet their future needs.

Baby Boomers, a name given to those born between 1946 and 1965, have been noted for their creation of the "computer age," quest for

physical fitness, and expectations for living long, full lives. Now, as Boomers pass into middle age, many are beginning to focus on retirement.

Many Boomers wonder if they can depend on receiving Social Security benefits during their retirement years. Indeed, some economists question the future "security" of the Social Security system. To add to this uncertainty, not all employed Boomers have **employer-funded retirement plans**. In today's workplace, the

responsibility for retirement saving has shifted from *employer* to *employee*. Consequently, personal savings may be more important than ever before.

What can Boomers do to determine if their savings and assets are sufficient to fund their retirement? Because no one really knows what the future holds, definitive answers remain elusive. However, Boomers may be able to gain more insight into their financial future by assessing the following key items:

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Understanding IRA Minimum Distribution Requirements

Many people who have been contributing to **Individual Retirement Accounts (IRAs)** for years have watched their account balances grow through tax-deferred accumulation. However, did you know the Tax Code mandates that contributions to traditional IRAs are no longer permitted after reaching age 70½ and **required minimum distributions (RMDs)** must commence no later than April 1 of the year after the year in which you reach age 70½?

Let's take a look at the following example. Suppose Bob's 70th birthday was July 15, 2012 and he attained age 70½ on January 15, 2013. Bob will have until April 1, 2014 (the year after reaching age 70½) to begin taking distributions.

It is important to note: The first RMD is actually for the year in which you attain age 70½; however, you are allowed to *postpone* it until April 1 of the following year. For every year after the first distribution, the RMD must be taken by December 31.

At first glance, postponing the first RMD may seem like a good idea because you can gain additional tax deferral. However, a second RMD would be due by December 31 of the same year (i.e., that year's required distribution). Not only would this substantially increase your taxable income, but it could also limit some deductions based on adjusted gross income (AGI) and possibly subject your Social Security benefits to taxation.

Consequently, some people find that it makes sense to take the first RMD in the year when age 70½ is reached, rather than to postpone and "double up" the following year.

Calculating the Distribution

Each year, the RMD amount is calculated by dividing the IRA balance, as of December 31 of the previous year, by the applicable life expectancy factor from the appropriate IRS table. If an individual has

more than one IRA account, the RMD amount must be calculated according to the total balance in all accounts. However, the amount can be taken out of any one (or more) IRA account. For each subsequent year, the RMD amount must be recalculated.

Note that if you fail to withdraw the RMD amount for each year, you may be subject to a tax penalty. This tax is 50% of the difference between the amount *actually* withdrawn and the amount *required* to be withdrawn (i.e., the minimum distribution shortfall).

IRAs continue to be valuable vehicles for retirement planning. However, the time of reckoning (i.e., mandatory withdrawals) may be approaching for many IRA owners. Knowledge of the rules may help avoid potential tax problems. Be sure to consult a qualified tax professional for advice specific to your unique circumstances. ■

baby boomers and the changing world of retirement

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- Potential income sources (income-producing real estate, inheritances, etc.)
- Projected retirement savings account balances
- Projected cost of future health care
- Projected annual rate of inflation
- Projected amount of Social Security income
- Percentage of present income required for retirement

- Length of years retirement may last or life expectancy

A 2012 survey conducted by the Employee Benefit Research Institute* found that only 14% of Americans are very confident they will have enough money to live comfortably in retirement. Results also revealed that only 42% of workers have tried to calculate how much money they will need for a comfortable retirement, and 60% reported that the total amount of

their savings (excluding the value of a home or defined benefit plans) is less than \$25,000.

As is true of every generation facing retirement, Baby Boomers need a disciplined savings program. With a personalized financial plan and commitment to save more, Boomers can work toward improving their financial outlook to make their retirement years golden. ■

* Source: *Retirement Confidence Survey*, Employee Benefit Research Institute, 2012.

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Once you have a sense of your goals, estimate your financial needs. Generally, a retiree's living expenses are roughly 30% less than his or her expenses during working years. While some costs may increase, such as health care and leisure activities, others may decrease. For example, retirees tend to spend less on mortgages and education.

Know Your Resources

The second step in preparing for your retirement is to determine from where you will attain your retirement money. Most people draw on three main sources of income during retirement: Social Security, employer-sponsored plans, and personal retirement savings. Each offers important resources that can add to your overall retirement savings.

With Social Security, the benefits received are based on the income you have earned over the course of your life, subject to a maximum amount. It offers, for most, only a base level of income. Therefore, many retirees supplement Social Security benefits with savings from employer-sponsored plans, such as pension plans, 401(k) plans, 403(b) plans, Simplified Employee Pensions (SEPs), and Savings Incentive Match Plans for Employees (SIMPLEs). The tax advantages and, in many instances, matching contributions



from employers make these savings vehicles popular complements to personal retirement savings, which often include traditional Individual Retirement Accounts (IRAs) and Roth IRAs.

Make a Plan

Now that you've thought about your retirement objectives and your potential sources of income, the last step is to develop a plan that helps you address any potential shortfall in your retirement savings. Analyze your current spending habits to find out where your money is actually going and how much you have available to put aside for retirement savings. It may be worthwhile to investigate ways in which you can

adjust your lifestyle to decrease spending, and thus increase the amount available for savings. Can you "nip and tuck" without detracting from your quality of life? Are there short-term sacrifices you are willing to make for long-term gain?

When it comes to preparing for retirement, stick to your plan, but be sure to monitor it regularly, as your needs may change over time. Make sure your disciplined approach to saving continues to meet your current and future goals. It's never too late to start saving. Put yourself in a position of working toward your retirement goals, as soon as you can. ■

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