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BFAS Money Line

PENSION PLANS

Critical Pension Decisions

Quite surprisingly, my clients seem to be getting older, usually at the rate of about one year per year. One consequence of that aging is that more and more clients are reaching age 59 ½ , when withdrawals from IRAs, Keoghs, 401(k)s, or pension plans become possible without paying the federal 10 premature withdrawal penalty. Also, more clients are reaching the age of 70 ½ and beginning to make mandatory withdrawals from those retirement plans.

At those times there are several decisions to be made that can have significant income tax and estate tax consequences. These decisions include when to begin withdrawals, how much to withdraw, and who to designate as the beneficiary of retirement funds.

Within retirement plans, investments can grow without current taxes, but when retirement plan assets are withdrawn, income tax is due on the amount withdrawn. For this reason, the standard strategy in retirement is to spend after-tax assets first and use retirement plan assets last, to postpone the income tax (and allow

tax-deferred compounding) as long as possible.

The standard strategy for selecting a beneficiary is to designate the surviving spouse, and select the distribution calculation method that results in the lowest required withdrawals. The spouse is usually the best beneficiary, especially because the spouse can roll assets to his/her own IRA with no income taxes, further deferring the day of reckoning with the tax man. You must remember, though, that income taxes will be paid ultimately, as there is no step up in basis at death for retirement plan assets.

At age 70 ½, you must select the method of calculating the minimum required withdrawals. You may select either the owner's life expectancy or joint life expectancy with the named beneficiary, usually the spouse. However, if a non-spouse is designated as the beneficiary, his/her age, used to calculate the minimum distribution, is deemed to be no more than 10 years younger than the owner.

In addition, you must elect whether to recalculate life expectancy every year, or use a term certain (non-recalculate) calculation method. The recalculation method results in lower minimum required withdrawals. However, if your spouse dies first, you must use your single life to recalculate the minimum withdrawal. After your death, your secondary beneficiary must receive the entire account (any pay income taxes in addition to estate taxes) by the end of the year following your death. If the term-certain method is used, the initial joint life expectancy calculation continues to be used for the required withdrawals after the death of you or your beneficiary, allowing distributions to be spread over a longer period, if desired, by the secondary beneficiary.

Virtually all elections should be joint, not single. Some experts recommend joint recalculate for the owner and term certain for the beneficiary.

When you reach age 70 ½, you'll also need to decide if you want to begin distributions in the same year, or wait until as late as April 1 of the following year. If you wait, you make two required withdrawals, and pay the taxes, in the year after age 70 ½.

About the only thing that is clear about selecting a method of calculating the required withdrawals is that **the irrevocable decisions made before the first required withdrawal after reaching age**

70 ½ are important decisions, and need to be custom-fitted to each person's individual situation. If you, or a loved one, will reach age 70 ½ this year, please discuss your choices with me in time to make a well-thought-out decision before the end of the year.

FINANCIAL PLANS

To Plan or Not to Plan?

Having a financial plan is the key ingredient behind saving for your financial goals.

That's the conclusion of a just-released study from the Consumer Federation of America (CFA) and NationsBank, which surveyed almost 1800 households earlier this year to determine major causes behind the so-called "savings crisis."

The big surprise of the study is that … **those with comprehensive financial plans save more money, feel better about their savings program and make more appropriate decisions about their investments**, " said Diane Colasanto, president of the Princeton Survey Research Associates, which conducted random interviews in January and February for the study. "Knowledge isn't as important as we thought it would be."

The study found that across all income levels, households with financial plans saved dramatically more money than those without plans. For example, for households earning between $20,000 and $39,999, the median total savings of planners is $28,500, compared to $14,300 for non-planners.

For households with incomes between $40,000 and $99,999, the planners have saved $89,650, versus $41,500 for non-planners. For households in the higher income brackets, planners save an average of 60 percent more than non-planners.

Sixty-one percent of planning households said they had some money set aside for each financial goal, compared to 36% for those without a plan.

INVESTMENTS

Stick Your Head in the Sand?

In an April 1st article (pg C-1) in the Wall Street Journal, Jonathan Clements focuses on the new frontier of behavioral finance – how to act rationally when the market seems to be falling apart. For instance, Richard Thaler, of the Univ. of Chicago, suggests that instead of focusing on our losses, we consider the money we've made recently and keep the faith. He and other behavioral finance researchers have found that **people suffer more pain from losses than they get pleasure from gains**, which tends to make them miserable if they follow the market day-to-day, since there are almost as many down days as up. Advice? Don't follow the market day-to-day. Stick your head in the sand.

Can't do that? Meir Statman, Thaler's counterpart at Santa Clara Univ., suggests that investors set up a mechanistic line of defense. Always wait a week before taking investment action, so you don't do anything impulsive. Or always discuss a trade with your spouse or a friend.

Deena Katz, who practices in Coral Gables, Florida, suggests that you focus, not on losing money but on the **dangers of losing your lifestyle**. The **threats to your lifestyle**, of course, **are inflation and taxes**, which have nothing to do with short-term stock market volatility.

Clements also finally gets around to diversification, and tells us to ignore the dire predictions that come when the market seems to falter. Then he gives a **short-term forecast** that is truly priceless: "**I haven't the foggiest idea**."

HEALTH INSURANCE

Many of you remember the discussion of MSA heath care plans for small businesses in my last newsletter. Congress said they would halt new plans once 750,000 plans were in place. They would look September 1st to see how many were in force. Recent tallies show over 4 million in place. So those of you on the fence need to make a decision by September 1st or kiss this opportunity good-by until/unless Congress re-authorizes MSAs.

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