Are You Prepared for Retirement?

by Deborah O'Neil

I am going to answer a question with a question: What day of the week do you spend more money—Wednesday or Saturday?[1] Many of us can answer this without much thought. It is almost always Saturday.

Consider this: During retirement every day is a Saturday, with time to play, enjoy, learn, and create new experiences. This applies even to those of us who hope to continue working with a reduced schedule; there is a lot more time to enjoy life, which, depending on your activities, can require more cash and resources. Unfortunately, fewer than half of all investors have tried to calculate how much they'll need in retirement.[2]

Assessing Your Needs

So, are you prepared for retirement? To be prepared, you likely would have:

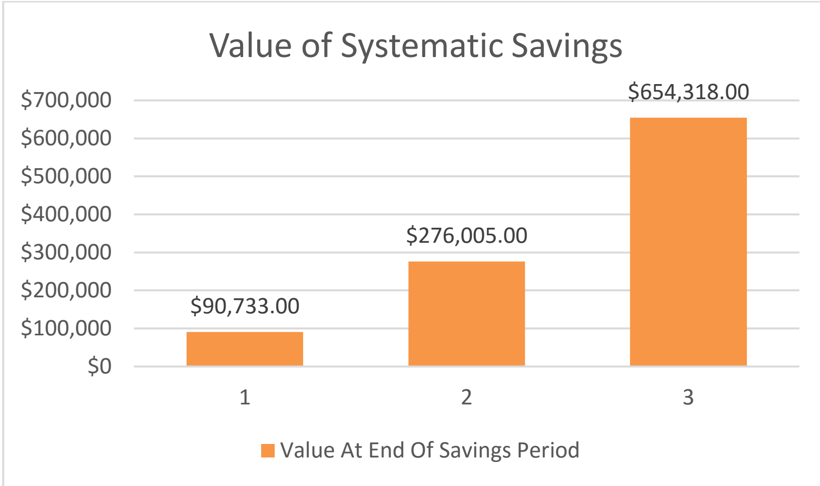
- identified your monetary needs during retirement, including living expenses, projected healthcare costs, and any discretionary spending you would like to have;
- calculated what your current retirement accounts and savings are projected to grow to at the point of your retirement, using a reasonable growth rate based on your current asset allocation; and
- chosen a path to make up for any shortfall so you can retire the way you want to.

If you are like many professionals, you are busy working and building your business. Your plan is to start planning for retirement tomorrow, next month, or next year. However, the value of starting *now* cannot be minimized. The chart below shows what happens when an individual saves $500 per month in a tax-deferred retirement account for the periods noted. The account has a hypothetical growth of 7.4% compounded annually.[3]

Scenario 1—10 years

Scenario 2—20 years

Scenario 3—30 years



The above does not represent the performance of a specific investment and does not take into account the effect of fees, commissions, and inflation. Individual investor results and tax ramifications will vary. Asset Allocation is a method of diversification which positions assets among major investment categories. This tool may be used in an effort to manage risk and enhance returns. However, it does not guarantee a profit or protect against a loss

There is an often quoted statement by Albert Einstein that "[c]ompound interest is the eighth wonder of the world." And that is exactly the phenomenon that occurs in a retirement account that grows tax deferred for many years.

Getting Started

Saving for retirement doesn't have to be complicated. To get started, find out whether your firm offers a retirement plan for employees and if you are eligible (some employers have a waiting period for new employees). If so, you should identify your budget and immediately start deferring funds to the account. The goal is to defer enough to get the maximum employer match, if there is one available, and then increase your deferral annually, if you can. Eventually you will want to defer the amount necessary to meet your retirement goal, using your projected hypothetical growth rate.

If your firm does not have a retirement plan, a good place to start is by opening a traditional IRA or a Roth IRA which can be completed with a financial advisor or your bank. For 2017, the contribution limit for both of these individual plans is $5,500 per year. If you are age 50 or above, you can contribute an additional $1,000 per year.

Traditional IRAs have no income limits. As long as you have earned income and are under age 70½, you can make a contribution to a traditional IRA. However, for contributions be tax-deductible, you must meet certain income requirements. See IRA Deduction Limits

Roth IRAs are funded with after-tax contributions, and the distributions are tax free if certain requirements are met. See Roth IRA However, unlike traditional IRAs, your modified adjusted gross income (AGI) affects whether you can contribute the maximum amount or are excluded from contributing altogether. Income eligibility requirements for Roth IRAs are:

- Single taxpayer—phase out begins at $118,000 AGI and is unavailable at $133,000 AGI.
- Married filing jointly taxpayer—phase out beings at $186,000 AGI and is unavailable at $196,000 AGI.

In general, Roth IRAs are considered a good choice for those who expect their tax rate to be higher in retirement, while traditional IRAs benefit those who expect their tax rate to be lower in retirement however, each person's individual situation should be reviewed to identify the appropriate option.

Choosing a Plan for Your Firm

If you're a firm administrator is considering setting up a retirement plan for your firm, there are several types of retirement plans to choose from. Each has advantages and disadvantages.

The accompanying table shows some general characteristics of different types of employer-sponsored retirement plans that are available to solos and multi-attorney firms.

	Employer Contribution Limits	Individual Contribution Limits	Catch-up Contributions Age 50+	Roth Contributions Allowed	Who Directs Investments	Third Party Administrator Needed
Simple IRA	Must match $1 for $1 up to 3% of income[1]	$12,500	$3,000	No	Individual	No
SEP	Up to $54,000[2]	None	None	No	Individual	No
Solo 401k	Up to $54,000[3]	$18,000	$6,000	Yes	Individual	No[4]
401k	Up to $54,000	$18,000	$6,000	Yes	Individual	Yes
Cash Balance Defined Benefit	Based on income up to $215,000	None unless it also has a 401k feature	None unless it also has a 401k feature	No	Employer/ Trustee	Yes
Defined Benefit	Based on income up to $215,000	None	None	No	Employer/ Trustee	Yes

Notes

1. Alternatively, the employer can contribute 2% of compensation for all eligible employees whether they defer/contribute to the plan or not.
2. Not to exceed 25% of compensation.
3. This amount is reduced by any individual contributions.

4. Once the balance reaches $250,000, a third-party administrator may be needed for reporting and testing, as an IRS Form 5500 is required.

Regardless of which type of plan you are considering; the following steps can help guide you through the decision-making process and beyond:

- Identify the firm's goals.
- Calculate the firm's budget for the benefit.
- Specify who in the firm will be responsible for the fiduciary and compliance requirements.
- Partner with a financial professional who can identify various plans and discuss the advantages, disadvantages, costs, and steps.
- Choose the plan that fits the firm.
- Distribute required disclosures.
- Educate employees about the plan benefit and investment options (your financial professional will do this for you) and conduct enrollment meetings.
- Schedule annual employee meetings for your financial professional to review general retirement planning information and investment options, and ensure annual disclosures are sent.
- Review your financial professional's market analysis every two to three years to ensure it is still competitive in the marketplace and appropriate for the size of the firm and the account.

Whether you are implementing a retirement plan or updating your current one, select a plan that meets the unique attributes of your firm. Be confident you have taken steps for yourself and your employees to prepare for retirement.

Conclusion

Employer sponsored retirement plans can be a great benefit for the owners and employees as long as the plan remains current with the goals of the business and the plan continues to meet the fiduciary and regulatory requirements.

---

1. Hegna, *Pay Checks and Play Checks: Retirement Solutions for Life* (Acanthus Pub. 2011).
2. Helman et al., "2013 Retirement Confidence Survey: Perceived Savings Needs Outpace Reality for Many," Employee Benefit Research Institute (2013).

3. 7.4% is a hypothetical growth rate based on a diversified portfolio's return between 1996 and 2015 with an allocation of 35% Barclays US Aggregate Bond Index, 10% MSCI EAFE Index, 10% Russell 2000 Index, 22.5% Russell 1000 Growth Index, and 22.5% Russell 1000 Value Index. It assumes reinvestment of all distributions. It is not possible to directly invest in an index. Diversification does not guarantee a profit or protect against loss.

Deborah O'Neil, JD., LL.M., CFP®, CLU is Vice President with Assured Equity Management Corporation and works with individuals and privately owned companies. For additional information or questions please contact Debbie at 303-785-7681 or doneil@assured-equity.com Securities offered through AXA Advisors, LLC (NY, NY 212-314-4600), member FINRA, SIPC. Annuity and insurance products offered through AXA Network, LLC. AGE-122094(01/17)(Exp.01/19)

This article was originally published in *The Colorado Lawyer* – Vol. 46, No. 3, March 2017.