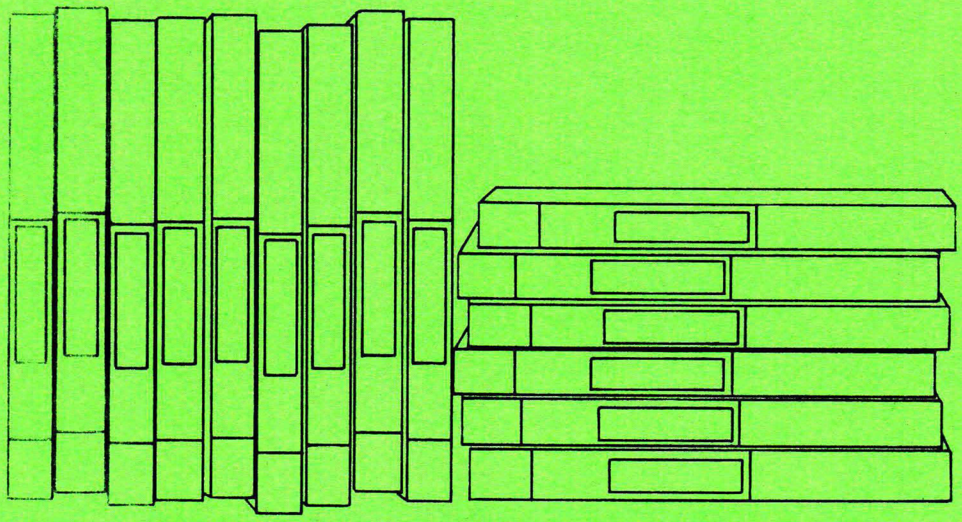

THE FAMILY FINANCIAL LIBRARY

PLANNING AND MANAGING YOUR RETIREMENT

A Consumer's Guide to Growing Older with Money

1. *Understanding the Economics of Retirement*
2. *Preparing for Your Retirement*
3. *Determining the Best Time to Retire*
4. *Managing Your Retirement Resources*
5. *Protecting Your Health*
6. *Preserving Your Estate*

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UNDERSTANDING THE ECONOMICS OF RETIREMENT

<u>**Time and Money Passing On.**</u> It's difficult for most pre-retirees to really appreciate the economics of retirement. Many envision retirement as a time of personal enjoyment and freedom from work. Most of us envision the lifestyle we hope to enjoy in our early or mid-sixties and hold this vision as a lasting reflection of our retirement years. Unfortunately, the early years of retirement do not last and neither do the conditions which may prevail during that period. The following is an exercise to help you to broaden and deepen your understanding of your retirement years.

			Example
1.	To what age do you expect to live?	______	85
2.	At what age do you hope to retire?	______	65
3.	Subtract 2 from 1 for answer 3.	______	20

Answer 3 is your estimated length of retirement.

4.	What is your current age?	______	45
5.	What is your answer to 3 above?	______	20
6.	Subtract 5 from 4 for answer 6.	______	25

Answer 6 is how old you were when someone just like you began a retirement of your anticipated length.

Answer the following questions in order to experience something of the economic change that would affect a person's life over such a period of retirement.

7.	In what year were you the age noted above?	______	1968
8.	What was your/your family's annual income?	______	$6,300
9.	How much was a week's groceries?	______	$25
10.	How much was the monthly rent/housing cost?	______	$75
11.	How much did your/your family's car cost?	______	$1,300
12.	How much did a gallon of gasoline cost?	______	$ .25

THE AGES AND STAGES OF RETIREMENT

<u>Retirement is not a point in time; it is a period of time.</u> As such, it is subject to significant changes. Typically, we tend to minimize the extent of the time and changes involved. The "ages and stages of retirement" indicated below serve to remind us of the broad differences in perspective associated with time.

EARLY RETIREMENT (Ages 60-70)*

Major Concerns	Cost of Living	
1. When's the best time for me to retire?	**60**	**$20,000**
	62	22,472 **
2. What will I do when I retire?	65	26,765
	67	30,073
3. What should I do with my retirement funds?	70	35,817

MID-RETIREMENT (Ages 70-80)

Major Concerns	Cost of Living	
1. How can I protect my health?	**70**	**$35,817**
	72	40,244
2. Where should I live out my retirement?	75	47,931
	77	53,856
3. Are my financial affairs in order?	80	64,143

OLD AGE (Ages 80-90)

Major Concerns	Cost of Living	
1. How will I get around?	**80**	**$ 64,143**
	82	72,071
2. Will my money run out before I do?	85	85,838
	87	96,447
3. Who will take care of me if I can't take care of myself?	90	114,870

* Age Brackets Arbitrarily Assigned for Illustrative Purposes
** Cost of Living Increases Figured at 6 Percent Annually

CHECKLIST OF KEY CONSIDERATIONS FOR YOUR RETIREMENT

Check Your Greatest Interests or Concerns. See capsule comments on the pages which follow for specific information on each of the items you have checked.

PREPARING FOR RETIREMENT

______ 1. Exploring Your Employer's Contributory Plan
______ 2. Investing in Real Estate
______ 3. Investing in Deferred Compensation Plans
______ 4. Investing in an IRA
______ 5. Investing in Mutual Funds

DETERMINING WHEN TO RETIRE

______ 1. Impact on Social Security Income
______ 2. Impact on Pension Income

MANAGING RETIREMENT RESOURCES

______ 1. Handling Your IRA Rollover
______ 2. Making IRA Withdrawals
______ 3 Tapping Your Pension Income
______ 4. Cashing Your Life Insurance Policy
______ 5. Buying a Retirement Annuity
______ 6. Selling Your Home for Cash
______ 7. Drawing on a Reverse Mortgage

PROTECTING YOUR HEALTH

______ 1. Gaining Employer Coverage for Your Spouse
______ 2. Joining a Health Maintenance Organization (HMO)
______ 3. Buying a Medigap Policy
______ 4. Buying Long-Term Care Insurance
______ 5. Entering a Life Care Community

PRESERVING YOUR ESTATE

______ 1. Making a Will
______ 2. Setting Up a Living Trust
______ 3. Gifts and Title Transfers

PREPARING FOR RETIREMENT

Exploring Your Employer's Contributory Plan. Don't reject your employer's contributory pension plan out of hand. Such plans may not offer the most aggressive investment return on employee contributions withdrawn prior to retirement. However, such plans frequently offer advantageous benefits for those who have to or want to retire early. They may also offer lifetime benefits for the employee and sometimes the employee's spouse. Furthermore, what may seem like an either/or choice between selecting the contributory plan or taking your contributions and investing on your own may not be totally accurate. Employees come to realize that they can and need to do both by joining the contributory plan from the beginning and then starting their own retirement account later on with additional funds from increases in income.

Investing in Real Estate. A home is perhaps the greatest and most worthwhile investment most people ever attain. A home provides not only shelter and tax advantages but significant appreciation as well. This is especially true in Hawaii, where tremendous values can be accumulated in home appreciation. Few people think of their home as a retirement investment, but it is probably the biggest and best retirement investment most of us will ever make. The same can be said of other real estate. Rental property, in particular, offers significant advantages in terms of favorable taxing applied to income, interest and depreciation. The principle of leverage also enables both home and rental real estate to multiply the initial investment at a much faster rate than that of the total property's appreciation. Furthermore, tax-deferred real estate exchanges under Internal Revenue Code (IRC) 1031 enable individuals to trade equal or up in acquiring a retirement home in exchange for a rental property and reserving their pre-retirement home for their beneficiaries.

Investing in Deferred Compensation Plans. Deferred compensation plans such as SEP plans, 457 plans, 401(k) plans, and 403(b) tax-sheltered annuities provided by tax-exempt organizations and public schools enable eligible employees to make tax-deferred contributions of income to a wide array of qualified retirement plans. The amount which an employee can ordinarily contribute each year is limited, ($8,728-$9,500 for 1992) but is still far more than that allowed for regular IRAs ($2,000). Moreover, the amount contributed and the interest it earns escape income tax until withdrawn at retirement. See IRS publications 571 and 575 for further information.

Investing in an IRA. Individual Retirement Accounts enable all employees to contribute up to $2,000 per year to an IRA in which earnings accumulate tax-deferred until withdrawn at retirement. Employees not covered by an employer pension plan and whose incomes are under $25,000 if single or $40,000 if married may also claim a full income tax deduction on contributions up to $2,000. Uncovered employees whose incomes are between $25,000 and $35,000 if single and $40,000 and $50,000 if married may claim a partial income tax deduction on their IRA contributions. The advantages of tax-deferred contributions and earnings for eligible employees are obvious. However, even employees not eligible for tax-deferred contributions may contribute up to $2,000 each year of after-tax income to an IRA. The earnings of these contributions are tax-deferred. This enables most employees to add a program of tax-deferred investments to any other pension or retirement plan they might have. Moreover, any IRA may be set up as a self-directed IRA account with a discount broker at little or no cost. A self-directed IRA enables an employee to control and invest his own funds and and aggressively pursue his own retirement goals with what might be considered supplementary retirement contributions.

Investing in Mutual Funds. Mutual funds offer the average investor access to almost any type of investment there is and with some important advantages. Compared to other forms of investing, mutual funds are very easy to understand, evaluate, contribute to and make withdrawals from. Their investment goals and objectives, portfolio descriptions, records of performance, fees, manager's identity and phone numbers are easily obtained from selected issues of U.S. News & World Report, Business Week, Kiplinger's Personal Finance Magazine, Money, and other such magazines. Studies indicate that no-load or no fee mutual funds perform as well or better than those that charge fees to support their sales force. Mutual funds enable the average investor to invest fairly small amounts of capital in the broad portfolio of one fund and larger amounts of capital in the variety of portfolios of several funds. With this flexibility, the average investor can minimize risks, fees and complications associated with individual stock, bond and other security investments while enabling participation and reward in portfolios that may be super safe, very aggressive or anywhere in between. The rewards of mutual fund investing range anywhere from gains of 100% or more per year to losses in double digits. Consult the magazines noted above to check individual performance records and obtain 800 toll-free telephone numbers to request any fund's prospectus.

DETERMINING WHEN TO RETIRE

Impact on Social Security Income. Financially, the later you retire the better. Social Security income is computed on the basis of the number of quarters you worked and the amount of money you earned. A person who was 45 years old in 1989 and earned $45,000 or more in 1988 might receive **$15,084** adjusted for inflation upon retirement at age 66. If that person chose to retire at age 62, he would receive **$11,313** (75% of the full benefit) and this 25% reduction would continue for the future. On the other hand, if this same person delayed retirement beyond the normal retirement age, he would receive a credit of 8% for each year of delay. The current credit is 3% per year and this is scheduled to rise to 8% per year by the year 2009. Also, it should be noted that the normal retirement age is changing. It is 65 for those born in 1937 or earlier, 66 for those born between 1943-54, and 67 for those born in 1960 or later. To find out what your estimated social security benefit will be when you retire call 1-800-937-2000 to obtain a form entitled "Request for Earnings and Benefit Estimate Statement."

Impact on Pension Income. Pension income is also adversely affected by early retirement. Pension income is usually computed on the basis of three factors: (1) the employee's average salary over the last or highest paid three to five years of employment, (2) the number of years he or she was employed under the pension plan, and (3) the accrual rate specified in the plan. Thus, an employee with an average final salary of $50,000, 25 years of service and a 1.5% accrual rate would receive an annual pension at normal retirement age of 65 of **$18,750** (50,000 x 25 x .015). If the employee were to retire earlier, the pension benefit might be reduced by 5%, 6% or 7% for each year in advance of the normal retirement age. Furthermore, the average salary to be used in the computation might be considerably lower. If the employee above chose to retire three years earlier than normal retirement age, the average salary used might only be $44,000, the years of service 22, and the penalty assessed for each year in advance of normal retirement age 6%. Retirement at age 62 would mean a pension of $14,520 (44,000 x 22 x .015) reduced by 18% (3 x 6%). The resulting annual pension benefit of **$11,906** is 37% less than the normal retirement benefit, and this reduced benefit would continue for the duration of the retirement.

MANAGING RETIREMENT RESOURCES

Handling Your IRA Rollover. At the termination of employment, an employee may receive a lump sum distribution from his or her employer sponsored retirement plan. The distribution of tax-deferred contributions and earnings from a qualified plan are taxable when received. However, the employee can take steps to defer or minimize the applicable tax. The applicable tax will be deferred on this entire amount or any portion thereof if the employee rolls it over into another qualified retirement plan within sixty days of the distribution. However, the portion not rolled over will be taxed as regular income in the year in which it is received. On total distributions received in one year, employees who are age 59 1/2 or older may reduce their tax by using five-year or ten-year averaging. Averaging allows the tax liability to be figured on the basis of what would be owed if the money were received over a five or ten year period, but the whole tax is actually owed and paid in the year the distribution is received. Only those who receive a distribution of their entire retirement plan balance in one year and who do not roll over any part of it may use averaging. Moreover, only those who reached age 50 by January 1, 1986, may use the more favorable ten-year averaging. Applicable information and instructions regarding tax averaging are provided in IRS publication 575.

A new federal law that went into effect January 1, 1993, requires taxpayers to pay a 20 percent withholding tax when they elect to cash out a 401(k), 403(b) or other qualified, employer-sponsored pension plan. To avoid this withholding tax, taxpayers wishing to establish an IRA with their disbursement should have transfers made directly from their pension plan to their IRA. This rule does not apply to IRA disbursements or transfers made within the 60 day period allowed. The complexity and changeability of tax laws strongly suggests that taxpayers should seek the assistance of qualified tax specialists before making important decisions regarding any transaction or disbursement of retirement funds.

Making IRA Withdrawals. IRA withdrawals cannot be made until age 59 1/2 without incurring a 10% early withdrawal penalty on the part of the distribution that must be included in gross income. Exceptions apply in cases of disability, death, or loss of employment after age 55. Exceptions also apply where expenses for medical care exceed 7.5% of adjusted gross income. Also, IRA withdrawals must be made by age 70 1/2 in order to avoid a 50% penalty on the difference between the minimum withdrawal allowed and the amount actually withdrawn. The minimum withdrawal is

PROTECTING YOUR HEALTH

Gaining Employer Coverage for Your Spouse. Under some employer health plans, an employee must include a spouse under his or her health coverage a set number of years before retirement in order to lock in this spousal coverage after retirement. The period required may be three to five years. If the spouse is covered for this period of time before the employee's retirement, then he or she is eligible for coverage after his or her retirement. This is a particular concern in cases where both spouses work but are covered under separate plans. One employer's plan may not extend coverage beyond retirement for employee or spouse or it may offer it for the employee only. Another may extend coverage for both employee and spouse, but only if the spouse has been covered under the employee's plan for a stated number of years before the employee's retirement. Therefore, in preparing for your retirement, it is very important to check the conditions of your employer's health plan in order to determine what kind of coverage will be available to you and your spouse after you retire. If there are conditions to fulfill, you need to know what these are so that you can respond appropriately.

Joining a Health Maintenance Organization (HMO). HMOs provide health care by contract rather than health coverage by insurance. Usually, coverage is quite complete and out-of-pocket fees for services are minimal. Some HMOs even offer specialized plans for seniors that directly incorporate into their services and fees the coverage and benefits available to seniors under Medicare and some Medigap policies. Thus, the process of accessing covered health services is simplified and patients may be more encouraged and inclined to seek help as soon as they discover a problem and participate in preventive as well as curative health care. HMOs are not all alike in terms of quality and costs. Thus, consumers need to explore alternatives and use their best judgment.

Buying a Medigap Policy. Medigap insurance policies are designed to supplement the coverage offered by Medicare. As of July 1992, a confusing variety of Medigap policies was standardized into ten types of policies. Each type or "plan" provides a specific list of coverages, and only these ten plans, labeled A through J, may be offered by insurers. All ten plans cover six specific types of Medicare co-insurance, deductible and extended coverage. Plan A offers only this basic coverage. Plans B through J include the basic coverage plus specific additions. Medigap policies enable consumers to select coverage that supplements Medicare coverage, but the costs are not insignificant. The most inclusive policies may cost $2,500 or more per year. Plan B, which offers the six basic coverages plus Part A deductible coverage, appears to be the best deal for many consumers. Those that can afford more extensive plans may do so after assessing their individual needs and the costs involved. However, they should be wary of paying for additional coverages that promise little more than an even trade of insurance dollars for benefit dollars. The Sept. 1991 issue of Consumer Reports provides some tips on evaluating the various optional coverages. The July 1992 issue of Kiplinger's Personal Finance Magazine provides a table of the ten medigap plans along with a coverage and cost comparison of four plans.

Buying Long-Term Care Insurance. Good long-term care insurance is very costly and only those with substantial assets to protect and the ability to pay up to $3,000 or more per person per year for life should consider buying it. Policies that offer low per day and maximum benefits relative to current and projected costs do not make good economic sense. Nor do policies riddled with limitations, restrictions and requirements that seriously erode the coverage provided and the possibility that benefits will be paid to the insured. For example, policies that do not pay for any custodial care or custodial care offered only within a skilled care setting are seriously flawed. So are policies which require demonstration of organic causes before extending coverage for dementia. Of course, policies which require prior hospitalization as a condition of eligibility for benefits are seriously flawed. They are also prohibited in Hawaii, although such a provision can be found in policies sold before December 1991. From an economic perspective, policies offering benefits of $50 per day with a lifetime maximum of $60,000 are seriously deficient in a market that requires $120 or more per day and up to $45,000 per year for institutional care now and who knows how much more later on when your actual claims are made. Consumers should be very wary of low-cost, low-coverage policies, and they should study the written provisions of any policy they consider very carefully. Only written provisions guarantee coverage and benefits. According to Hawaii's free look provision, a consumer has thirty days to return and cancel any long-term care policy for any reason whatsoever and receive a full refund of premium.

Entering a Life Care Community. A life care community offers aging retirees the opportunity to secure a home, a way of life, and whatever physical care they may need for the rest of their lives in exchange for a substantial entrance fee and monthly service fees. As a rule, life care communities are expensive. But they are worth considering for those individuals who own a substantial asset to tap, like a house, and have no one to take care of them in their old age. A life care community provides direct services, security and peace of mind--at a price. Those interested in further information and a directory of providers can write to AARP or The American Association of Homes for the Aging, 1129 20th St., N.W., Suite 400, Washington, D.C. 20036.

PRESERVING YOUR ESTATE

Making a Will. A will enables you to pass on your estate to your beneficiaries according to your wishes. It also enables you to protect your estate from unjust claims. The probating of a will ensures that your estate will be settled under the supervision and protection of the court. The preparation of a will under the guidance of competent legal counsel frequently leads to the correction of misguided plans and strategies and potentially harmful situations which could adversely affect the distribution of your estate and increase the costs involved. Even individuals who take advantage of a living trust in making their estate plan do so in combination with a will (a pour-over will) that covers items and contingencies not covered in the trust. A legally formulated and executed will is a basic and essential component of any estate plan.

Setting Up a Living Trust. A living trust enables you to pass on your estate directly to your beneficiaries without it passing through the fees, delays and legal requirements of probate. It also allows you to minimize or avoid estate taxes, which can be substantial. Moreover, provisions can be employed to ensure that your share of the marital property passes on to your children or stated beneficiaries even if your spouse should remarry and take on competing interests. Estate taxes are only applied to estate values in excess of $600,000. However, the tax is 37% or more of the amount in excess of $600,000, and the value of the estate is assessed at the time of death. Thus, given the current average home value and rapid rates of appreciation in Hawaii, most home owners here are in danger of exceeding the $600,000 limit within their lifetime. A home with a current market value of $300,000 could easily be worth more than $600,000 within ten years.

Gifts and Title Transfers. Gifts of up to $10,000 per person per year are excluded from tax. Amounts above the $10,000 exclusion may not be taxed immediately but are counted against a $192,800 (1987 and later) unified tax credit on gifts over one's lifetime. A gift tax return Form 709 or 709-A must be filed with the IRS by April 15 following the year the gifts are made. Title transfers are also used to bestow gifts. However, simply putting your son or daughter's name on a joint bank account does not automatically constitute a gift of the value held in the account. It does to the extent that the child takes possession of the money and uses it. Gifts and title transfers are common ways of transferring property, but they ought to be used with care. Transferring the ownership of a home to a son or daughter can and has resulted in the eviction of a giving parent on more than one occasion. Also, if received as a gift, the basis for computing capital gains on a home goes back to the basis of the parent rather than the value or "step-up basis" at the time of the parent's death, as is the case for transfers conducted by will or trust.

RECOMMENDATIONS FOR GROWING OLDER WITH MONEY

Preparing For Retirement

Carefully Consider Employer's Contributory Pension Plan
Invest in Real Estate for Long-Term Gains
Take Advantage of Deferred Compensation Plans
Supplement Your Plan with a Self-Directed IRA
Learn to Invest In Mutual Funds
Keep Good Records of Income And Investments
Retire Later Rather Than Sooner
Plan for the Future

Managing During Your Retirement

Plan Your Pension and IRA Withdrawals with a Qualified CPA
Roll Over Your Retirement Funds into Qualified Investment Plans
Use Taxed Resources before Tax-Deferred Resources
Consider Purchasing a Guaranteed Payment Annuity
Cash Your Life Insurance Policy for Health and LTC Protection
Make Contingency Plans for the Sale of Your Home
Don't Postpone Your Most Important Retirement Plans
Recognize Your Peak of Health May Not Last

Coping With Old Age

Adjust Your Lifestyle to Your Changing Capabilities
Consider Curtailing Some Activities and Beginning Others
Shift Your Expectations and Energies to Support Your Lifestyle
Manage Your Money Carefully
Ask for Help Where Needed
Prepare Your Family for Your Needs
Appreciate What You Can Do and Do What You Want to Do
Take More Naps and Suffer Fewer Fools

HOW ~~NOT~~ TO GROW OLDER WITH MONEY IN 20 EASY LESSONS

1. Hire unlicensed contractors who come to your door.
2. Trust someone else to manage your money for you.
3. Invest in things you don't understand.
4. Buy long-term care insurance without studying the policy.
5. Make undocumented loans to family members.
6. Give ownership of your home to your children.
7. Assume financial responsibility for your adult children.
8. Buy a $1,500 vacuum cleaner.
9. Close out lines of credit you're no longer using.
10. Use a storefront tax preparer rather than a CPA who specializes in taxes and tax preparation.
11. Move your life savings from slow but sure investments to limited partnerships and other high risk ventures.
12. Delay estate planning until you're really old.
13. Refuse to charge your adult children room and board.
14. Make absolutely no contingency plans to sell your home and move somewhere else if you have to.
15. Hang on to your life insurance policy until the day you die.
16. Take advantage of long-distance callers offering you free trips and other prizes you have been lucky enough to win.
17. If you get married again, be sure to put all of your assets in your name and that of your new spouse.
18. Use a will rather than a living trust to pass on your estate if your estate is worth anything less than $600,000.
19. Attend seminars on extraordinary investment opportunities.
20. Don't make any plans for the future. Just let it happen.

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