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21st century retirement

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Retirement Savers Value Lifetime Income Guarantees

As many Americans lack confidence that they will enjoy a financially secure retirement, significant shares say that having a guaranteed lifetime income is one of their top retirement planning goals, the results of a recent survey conducted by financial services provider TIAA indicated.

Published on September 23, TIAA's "2019 Lifetime Income Survey" includes responses from 901 Americans between the ages of 25 and 73 who completed an online questionnaire in May and June 2019. The aim of the survey was to uncover the factors that contribute to and detract from people's financial confidence, and to assess their attitudes toward financial products that can guarantee lifetime income.

When asked about their confidence in various financial aspects of retirement, just 35% of respondents expressed a high level of confidence that they will be able to maintain a good standard of living throughout retirement; 31% said they are very confident that they will feel financially secure throughout their life, including in retirement; 28% said they are highly confident they will never run out of money in retirement; and, of the respondents who are still working, 25% indicated they are very confident that they will be able to retire when they want to.

Broken down by generation, the survey results showed that baby boomer respondents expressed far higher levels of confidence in their financial preparation for retirement than younger respondents, with Generation X respondents reporting even lower levels of confidence than millennials. For example, while 53% of baby boomers said they are confident that they will be able to maintain a good standard of living in retirement, just 28% of millennials and 22% of Gen Xers indicated that they feel equally confident.

The survey also asked respondents how concerned they are about certain financial events occurring. The results indicated that the majority of the adults surveyed are worried about a major unexpected expense (54%), a major medical expense (53%), and significant cuts to Social Security and Medicare (53%); and that significant shares are also concerned about a major market decline (45%) and an increase in inflation (41%).

In addition, the findings indicated that of those respondents who participate in an employer-sponsored retirement plan, 69% cited guaranteed income for life as one of their top two goals for their retirement plan, and

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SEC Alert: The Pitfalls of 401(k) Debit Cards

According to the U.S. Securities and Exchange Commission (SEC), 401(k) plan participants may want to exercise caution if offered a 401(k) debit card by their employers. A 401(k) debit card typically allows retirement plan participants to borrow up to $50,000 or 50% of the value of their retirement plan, whichever is less, through use of a debit card. But, a 401(k) debit card is not like a debit card that deducts money from a checking or savings account. Instead, early withdrawals from 401(k) accounts are loans that employees make to themselves out of their own retirement savings.

Just as with traditional credit cards, you must repay the money you withdraw using the 401(k) debit card, along with fees and interest, or you may incur substantial penalties. The SEC recommends that plan participants consider a number of factors before using a 401(k) debit card, including possibly having to pay interest and fees on amounts they borrow from their 401(k) accounts. While noting that some of the interest paid by borrowers goes back into their 401(k) accounts, a so-called "margin" may generally be paid to the vendor of the card. A number of additional fees may also be applied, including an annual fee, a set-up fee, a cash advance fee, and fees for other services, such as express delivery.

If borrowers fail to pay the money back in the time period required by the plan, there may be significant penalties and tax consequences. Under IRS rules, 401(k) plan participants who borrow from their accounts are typically required to repay the amount of the loan in five years or less, and cannot fail to make payments for three consecutive months. Borrowers who don't meet those conditions may owe taxes on their loan balance, and borrowers under age 59½ may also have to pay a 10% income tax penalty.

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retirement savers value lifetime income guarantees

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45% said that guaranteed income for life is their top goal. Researchers pointed out that the respondents were more likely to rank having a guaranteed lifetime income as one of their top two goals than keeping their savings safe regardless of what happens in the market (56%), earning a competitive rate of return on their savings (46%), or saving a specific amount of money (28%). Among the reasons the respondents cited for valuing an investment product that provides guaranteed lifetime income were that it gives them a feeling of financial security (60%), and that it makes it easier to save for retirement (46%).

When asked to name the factors that most increase their long-term financial confidence, the leading factor cited by respondents was saving regularly (40%), with smaller shares mentioning saving aggressively (21%), understanding how to pay down their debt (20%), receiving a guaranteed lifetime income from a traditional pension plan (18%), and having diversified investments (15%). However, 52% of respondents admitted that they did not save as much as they should have in 2018, including 22% who indicated that they saved a lot less than they should have.

The findings also suggested that while Americans value knowing how much income they will have in retirement, there is still considerable confusion surrounding financial vehicles that guarantee lifetime income. The survey found, for example, that 32% of respondents who indicated that they have an employer-provided retirement plan said they do not know whether their plan offers an investment option that guarantees lifetime income; and that among those who said they think that guaranteed lifetime income is available in their plan, significant shares demonstrated that they incorrectly believe that mutual funds (35%) and target date funds (20%) secure lifetime income.

When questioned about their sources of financial advice, the respondents were most likely to report that they rely on a professional financial advisor (36%), followed by their employer or retirement plan provider (32%), their spouse or partner (29%), and online retirement or income calculators (27%). The survey found that those respondents who indicated that they rely on a financial advisor expressed more confidence in their ability to always be financially secure, never run out of money, and maintain their lifestyle in retirement than those who said they do not. ■

sec alert: the pitfalls of 401(k) debit cards

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The SEC warns employees that the amounts set aside to borrow may earn a lower rate of return than the rest of their 401(k) assets. This is because funds the participant may wish to borrow are often placed in a money market fund, which usually produces lower returns than other 401(k) plan investment options, such as mutual funds or stocks.

In addition, the SEC cautions employees that, unlike 401(k) contributions, repayments of 401(k) debit card loans are not automatically deducted directly from payroll. Instead, borrowers need to take action to repay the balance.

Withdrawing money from your retirement account under any circumstances, including with a 401(k) debit card, should be carefully considered. Remember to weigh all the pros and cons, so you can make an informed decision. ■

Divorce and Retirement Plan Proceeds

because divorce usually involves the division of assets, including some that may have tax implications, it is important to be aware of potential "tax traps," such as **vested account balances**, when you begin your retirement planning strategies.

In the past, with traditional **defined benefit plans**, such as company pension plans, participants generally received a retirement benefit, but they had no vested balance in an individual retirement account. In other words, employees had no rights to the employer's contributions to the retirement plan. However, with the popular shift toward workplace **defined contribution plans**, such as the 401(k), contributions made by employees to their retirement plan are always vested, and employer contributions vest over time, according to the schedule set forth in the plan document. Consequently, dividing vested retirement plan assets in divorce proceedings has become a complex financial issue.

Protect Yourself with a QDRO

A **qualified domestic relations order (QDRO)** is a judgment or order that involves child support, alimony, and property rights pertaining to a spouse, former spouse, child, or other dependent. A QDRO can be used to establish one spouse's right to part or all of the other spouse's retirement plan(s) and ensure that the recipient spouse pays the tax.

To be protected through a QDRO, it must specify the following:

- The name and address of the plan participant and the "alternate payee" (typically, the participant's spouse).
- The name and account number of each retirement account involved.
- The percentage (or dollar amount) of each plan that is to be paid to the alternate payee.
- The period of time or the number of payments covered by the QDRO.

The QDRO must be a part of a divorce decree or a court-approved property settlement document. The decree must also specify that a QDRO is being established under Section 414(p) of the Internal Revenue Code (IRC) and the particular state's domestic relations laws. Intent to establish a QDRO is insufficient; it must be documented in the divorce papers.

Getting divorced can be "taxing" enough, so be sure that you understand the process of dividing retirement plan assets. Through a QDRO, an individual can provide retirement funds for a former spouse, child, or other dependent, and ensure that those assets are taxed appropriately. Consult your qualified tax and legal advisors for guidance on your unique situation. ■

Planning for a Social Security Shortfall

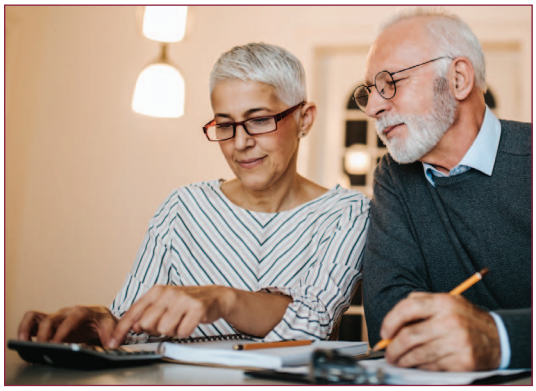
The Social Security program offers a retirement benefit to workers and their spouses. You can start receiving benefits as early as age 62, which would be considered early retirement, or wait until you reach the **full retirement age** of 65 to 67 (depending on your year of birth). The benefits you receive are based on the income you earned over the course of your working life, and are subject to a maximum amount.

What you may not realize, however, is that Social Security was not originally designed to be a retiree's sole source of support. For most people, Social Security provides only a base level of income. The maximum benefit for a person who retires in 2020 at full retirement age is $3,011 per month. Therefore, it is important to plan for retirement by preparing to supplement Social Security.

Here are some important savings strategies that may help you reach your retirement funding goals.

Participate in your employer's retirement plan. Regular contributions to an employer-sponsored retirement plan, such as a **401(k)**, can be an essential part of your retirement savings program. Contributions to such plans offer three key benefits: they are made with pretax dollars; they reduce your current taxable income; and they have the potential for tax-deferred accumulation. Generally, these plans allow you to set aside a percentage of income each year, up to a maximum amount.

Open a traditional Individual Retirement Account (IRA). Contributions to a traditional IRA may be tax deductible, depending on your participation in an employer-sponsored retirement plan, your adjusted gross income (AGI), and your tax filing status. Potential earnings accumulate on a tax-deferred basis. For tax year 2020, you can contribute up to $6,000 (or $7,000 for individuals age 50 or older). Contributions are limited to the amount of earned income and the owner must be under age 70 ½ at the end of the year. If funds are distributed prior to age 59½, a 10% Federal income tax penalty may apply, unless certain qualified exceptions apply.



Consider a Roth IRA. Contributions to a Roth IRA are not tax deductible; however, qualified distributions, including potential earnings, are tax free if you have held your account for at least five years and are over age 59½. Like a traditional IRA, you can contribute $6,000 ($7,000 for individuals age 50 or older) to a Roth IRA in 2020. Contributions are limited to the amount of earned income. Note that the limit applies to the total of all IRAs that a person may hold in a given tax year. Contributions phase out for single filers with AGIs between $124,000 and $139,000 and for married joint filers with AGIs between $196,000 and $206,000, in 2020. Withdrawals made prior to age 59½ may be subject to a 10% Federal income tax penalty, unless certain qualified exceptions apply. *Note:* A nonworking spouse can fund an IRA or Roth IRA based on the earned income of the working spouse.

Purchase a fixed annuity. Because an annuity is not subject to income limitations, it can be a valuable addition to your long-term savings program. With a fixed annuity, premium payments accumulate on a tax-deferred basis, and you receive a guarantee that your money will earn interest at a specified rate and that your return (the money paid back to you) will occur on a set schedule in fixed amounts. In general, annuity payments are guaranteed by the issuing company and are based on that company's continued ability to pay claims.

It is important to plan for retirement by preparing to supplement your Social Security benefits. With a disciplined approach to saving, you will be on track to enjoying the retirement you envision. ■

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