Retirement "Planning"

Typical Life Cycle

Birth ------------ Graduation day ----------------------------- Retirement day ---------------------- Death

Income:	Paper route		Regular paycheck		Social Security, pension etc.	
Expenses:	Student loans	Mortgage	Kid's college	Go-Go	Slow-Go	No-Go years

<<<<<<<<<<< Accumulation Phase >>>>>>>>>>> | <<<<<< Distribution Phase >>>>>

Known unknowns: Length of accumulation phase, distribution phase
Return on retirement portfolio, sequence of return risk, inflation, etc.
Unknown unknowns

Accumulation phase (assumes saving $15,000 per annum, 7% pa return)	Portfolio at age 65
Alan starts saving 15% pa at age 35, continues every year to age 65	$1,531,096
Betty starts at age 25, continues to age 35, then stops contributing	$1,688,048
Charlie starts at age 25, continues every year to age 65	$3,219,144

Distribution phase

Expenses: First cut = 80 % of final salary (No retirement plan contributions, commute expenses, SS taxes, etc)
Better to do a budget (Travel, increased medical expenses, long term care, etc.)
Calculate the shortfall after factoring in Social Security benefits, pension, etc.

Retirement portfolio needed is at least 25 times the annual shortfall (assuming Bengen's 4% rule)
But Bengen was probably optimistic (Derived in a bull market, assumed 35 year retirement)
Safer to use 30 to 50 times annual shortfall for retirement portfolio.
Save most of salary raises. Avoid "lifestyle creep".

Tax Diversification	**Tax-deferred plans**	**Tax-free plans**
Contributions:	Deductible	Not deductible
Distributions:	Taxable as ordinary income	Not taxed
Examples:	Traditional IRA	Roth IRA
	Spousal IRA	MyRA
	401(k) and 403(b) plans	Roth 401(k) and 403(b) plans

Contribution Limits	**2017**	**2018**
IRA	$5,500 (+ $1,000 age 50+)	$5,500(+ $1,000 age 50+)
SIMPLE	$12,500 (+ $3,000 age 50+)	$12,500 (+ $3,000 age 50+)
401(k), 403(b)	$18,000 (+ $6,000 age 50+)	$18,500 (+ $6,000 age 50+)

Required Minimum Distributions (RMDs)

Must start withdrawing from tax-deferred plans at age 70½ ; IRAs, 401(k)s, Roth 401(k)s, etc.
Does not apply to Roth IRAs.

IRS RMD tables

Table I Single Life Expectancy
For use by beneficiaries

Table II Joint Life and Last Survivor Expectancy
IRA Owner, spouse is sole beneficiary and spouse is >10 years younger.

Table III Uniform Lifetime
IRA owner
Unmarried, or Married and spouse is not beneficiary or not >10 years younger.

Roth Conversions

Convert traditional IRA to a Roth IRA

Owe taxes on deductible portions of contributions and on the earnings

Consider splitting the new Roth assets into two or more accounts with different asset classes

e.g. 30% Fixed income. 40% Domestic equity, 30% international equity

Can "recharacterize" (undo conversion) any/all accounts as late as tax filing date next year and then roll the remaining accounts into a single Roth account.

The "Backdoor" Roth: Can be used when MAGI exceeds Roth limits (Single = $133K, MFJ = $196K in 2017)

Make a non-deductible contribution to a regular IRA

Then convert the non-deductible IRA to your Roth IRA

Beware the IRS "pro-rata rule"; requires total of all IRAs be used to compute share of tax owed

Which account should I fund first?

1. Fund traditional 401(k) and 403(b) up to match limit (free money!)
2. Then contribute to Roth IRA up to limit
3. Back-door Roth IRA
4. Complete post-match funding of 401(k) and 403(b) plans
5. SEP IRA
6. Traditional IRA
7. Taxable brokerage account

Asset Location

Tax-efficient products which generate qualified dividends and long-term capital gains are best fit for taxable accounts e.g. muni bonds, ETFs, index funds, collectibles

Tax-inefficient products which generate interest, non-qualified dividends, and short-term gains are best in tax-advantaged accounts such as IRAs, Roth IRAs, 401(k) accounts.

Household asset allocation

	Tax deferred accounts e.g. traditional IRAs	**Taxable accounts** e.g. brokerage a/c	**Tax-free accounts** e.g. Roth IRAs
MMkt, T-Bills, CDs, etc.	*****	*	
Short-term bonds	****	**	
Long-term bonds	***	***	*
Large-cap domestic	**	****	**
Small-cap domestic	*	***	***
International stocks		**	****
Emerging markets		*	*****

Rebalancing: Use dividends, contributions, RMDs and other distributions first, then sale/purchase.

Estate Planning Issues

Federal estate tax exemption = $5.498M for 2018

But … be careful of income tax efficiency

Roth accounts are best; Heirs own no taxes, can stretch over their lifetime

Taxable accounts are good; Step-up in basis; no tax owed if sold immediately

Tax-deferred IRAs are worst; No step-up in basis; heirs owe ord. income tax on distributions

Consider leaving to charity. Qualified Charitable Distributions count as RMD.

Next month, January 10th, 2017: Managing your cash flow in retirement

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