MANAGING RETIREMENT INCOME

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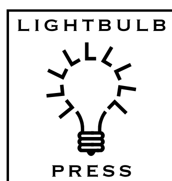

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Employer Plans

When you're mapping out the best route to collecting retirement income, there'll be several forks in the road.

If you'll have a pension or you've participated in a retirement savings plan where you work, and income from that source is a mainstay of your budget, the ideal solution is having your first retirement payment arrive the month after you receive your last paycheck. That requires making arrangements in advance.

On the other hand, you may not need the money right away. Then your goal is figuring out the best way to continue to take advantage of the potential for tax-deferred growth. Most plans offer a number of alternatives, and it's smart to investigate what they are.

THE CRITICAL FACTORS

While you don't have to decide until you're actually ready to stop working, making the best choice is critical. The factors you have to consider are your age and health, what you want to provide for your family, and what other sources of income you'll have.

For example, if you're in poor health and concerned about providing for your spouse, you might choose a joint and survivor pension annuity that will continue to pay while either of you is alive. On the other hand, if your spouse has a good pension from his or her employer or is seriously ill, you might choose a single life annuity that will provide a larger amount for you each month than a joint annuity would. In many cases, this option requires your spouse's written, notarized consent.

Or, if it's your employer's financial health you're concerned about, you may decide to take your money out of the plan and invest it elsewhere.

PENSION PLANS

When you retire from an organization that provides a traditional pension, you generally have two income choices: a pension annuity or a lump sum distribution.

With an annuity, you receive income each month for the rest of your life or your life and the life of another person, usually but not necessarily your spouse. At the time you retire, your employer calculates the amount you'll receive based on a number of factors including your age, your final salary, and the number of years you've worked for the organization. Income taxes are withheld from each check.

If you choose a lump sum, your employer calculates the amount you'll receive and transfers the money to an account you designate. If it's a cash account, income taxes are withheld, whether or not you plan to move the money into an IRA. If you roll over the amount directly to a tax-deferred IRA, income taxes are not due until you withdraw from that account.

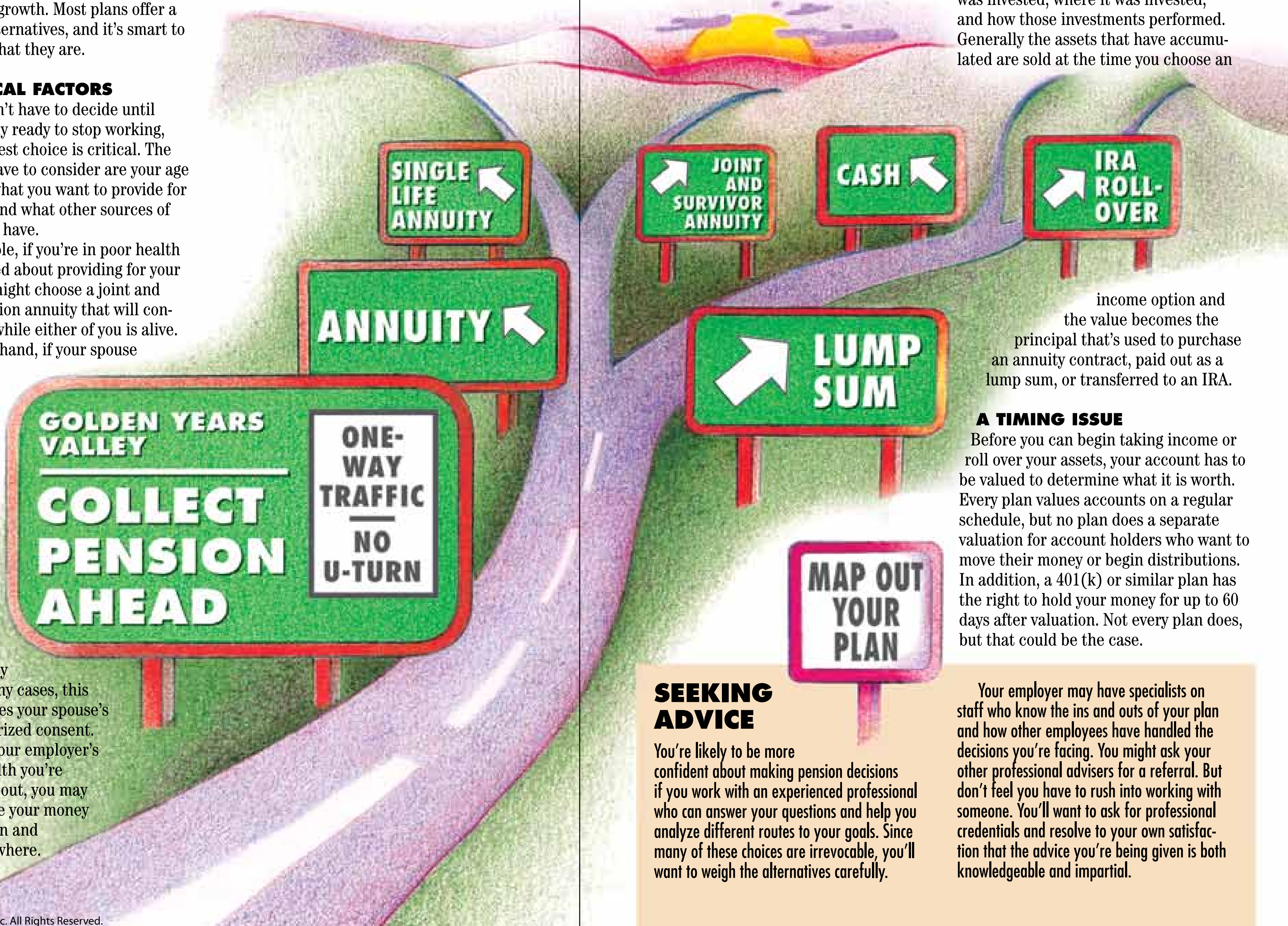
DEFINED CONTRIBUTION PLANS

If you're part of a defined contribution plan, such as a 401(k), 403(b), 457, or thrift savings plan (TSP), you have several choices for handling your plan assets. They always include (1) leaving your money in the plan, where you may be able to convert it to a pension annuity or take systematic withdrawals, (2) taking a lump sum, or (3) rolling over to an IRA.

Unlike a defined benefit pension, which pays your retirement income out of your employer's pension fund, retirement income from a defined contribution plan comes from assets held in your name. What you receive depends on how much was invested, where it was invested, and how those investments performed. Generally the assets that have accumulated are sold at the time you choose an income option and the value becomes the principal that's used to purchase an annuity contract, paid out as a lump sum, or transferred to an IRA.

A CORPORATE FIRST

Before the 1870s, retiring workers had to plan to live on their savings or depend on family. In 1875, American Express offered the first private pension plan in the US to employees over 60 who had been with the company for at least 20 years.



A TIMING ISSUE

Before you can begin taking income or roll over your assets, your account has to be valued to determine what it is worth. Every plan values accounts on a regular schedule, but no plan does a separate valuation for account holders who want to move their money or begin distributions. In addition, a 401(k) or similar plan has the right to hold your money for up to 60 days after valuation. Not every plan does, but that could be the case.

SEEKING ADVICE

You're likely to be more confident about making pension decisions if you work with an experienced professional who can answer your questions and help you analyze different routes to your goals. Since many of these choices are irrevocable, you'll want to weigh the alternatives carefully.

Your employer may have specialists on staff who know the ins and outs of your plan and how other employees have handled the decisions you're facing. You might ask your other professional advisers for a referral. But don't feel you have to rush into working with someone. You'll want to ask for professional credentials and resolve to your own satisfaction that the advice you're being given is both knowledgeable and impartial.

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Choosing an Annuity

You can control the flow of retirement income.

Deciding on a pension annuity is just the first step in converting your pension or retirement savings to a stream of income. Next is choosing how to take the income. One question is whether you want to provide income for one person or two. Another is whether it pays to reduce your income slightly to guarantee income will be paid for at least a minimum period. A third is whether you want income for life.

INFLUENCING

There are several key factors when you weigh the various payout options. It makes sense to review them with your financial adviser before making up your mind.

Who will get the money?

JOINT AND SURVIVOR OR **SINGLE LIFE**

Should the payout be life only or joint and survivor? For many people, wanting to provide lifelong income for a spouse or other beneficiary is the driving force in choosing a joint and survivor payout. Each individual payment amount is less than with a single life annuity, but the total over two lifetimes can be more, sometimes much more.

In most cases, if you're married and you decide against a joint and survivor payout, you'll have to provide your employer with a signed, notarized document from your spouse that gives his or her consent.

When isn't a joint and survivor policy the wiser decision? Among the factors to consider are how much income each of you has from other sources and how healthy you are. For example, if both you and your spouse have a good defined benefit plan, taking a single life annuity might make sense. It would provide more income than a joint and survivor payout, and your spouse is already guaranteed lifetime income. Similarly, if your spouse is ill, and unlikely to outlive you, a single life annuity might be the wiser choice.

What percentage should the survivor get?

50% OR **100%**

How much income should the survivor receive? The follow-up decision to choosing a joint and survivor payout is what percentage of the income that you receive while you're both alive should be paid to the surviving partner. There are usually several choices, with the least being 50% and the most 100%.

The decision involves trade-offs, as so many things do. If the surviving partner gets 100% of the income, the amount you get while you are both alive will be less. But the goal in choosing this alternative is that the survivor will have as much income as he or she needs.

On the other hand, an annuity paying the survivor 75% may provide sufficient income, since the living expenses of one person may be less than for two.

Whichever percentage, it will almost always be a better solution than an approach called pension maximization, or pension max for short. Here's how it works. You select a single life annuity and use some of the additional income to buy a life insurance policy to cover your surviving spouse's needs. But the death benefit will have to be invested, adding a level of responsibility that your survivor may not be comfortable with. What's more, the commission you pay to purchase the policy is likely to be substantial.

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INCOME ALTERNATIVES

Some pension annuities may provide a variable rather than fixed return, or a combination of fixed and variable. In either case, the income you receive each month will move up or down based on the performance of the investments underlying the variable portion. The advantage is that your income can increase, typically if the markets in which the variable portion is invested are strong. Conversely, the income may drop in periods when those markets stall or underperform as they tend to do periodically.

There are circumstances when knowing exactly what you can count on each month is more appealing than the potential for added income. But if you have a choice, it's something you may want to discuss with an independent financial professional.

FACTORS

How long will you get the money?

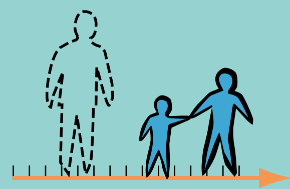
PERIOD CERTAIN OR **FIXED TERM**

Should you choose a life annuity that guarantees a certain number of payments? One reason people give for not choosing a pension annuity is that they're afraid if they die shortly after they begin receiving payments, they will forfeit a large portion of the amount they spent to purchase the annuity. To avoid that situation, some people choose a period certain payout guaranteeing that they or their beneficiaries will receive income for at least a minimum period, typically 5, 10, or 20 years.

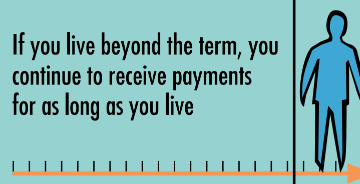
You can choose a period certain payout whether you take a single life or joint and survivor option. Although the guarantee reduces the amount you get somewhat, it provides added peace of mind and can be a wise choice.

PERIOD CERTAIN PAYOUT

If you die before the term is up your beneficiaries continue to receive payments



If you live beyond the term, you continue to receive payments for as long as you live



Should you take a payout that doesn't guarantee life income? If the reason you're choosing an annuity is being able to count on income for as long as you live, you should choose the lifetime guarantee. But there are situations when getting a larger amount of money each month or ensuring payments will last a specific amount of time may be a better decision.

What's appealing is that these payout models can produce the largest income payments in the short term. Also, when you select this option, you typically have the opportunity to **commute**, or cash in, your annuity for a lump sum after you've started to receive income rather than continue to receive income payments in the future.

PROTECTING YOUR ASSETS

If you're in debt when you retire, leaving your retirement assets with your employer and selecting a pension annuity probably makes more sense than a lump sum withdrawal. That's because federal ERISA law protects plan assets from most personal and professional claims but doesn't protect cash you withdraw.

In most cases, you can't be forced to withdraw, nor can your account be frozen until you pay your debts. There are exceptions. If you owe child support, alimony, or federal income taxes, you may be ordered to withdraw. So it always pays to seek legal advice from an attorney who specializes in ERISA matters.

You'll also want to confirm that assets you roll over to an IRA will be shielded by federal law in the same way as assets that remain in your plan before you consider moving the money.