COOPERATIVE EXTENSION SERVICE

VIRGINIA POLYTECHNIC INSTITUTE AND STATE UNIVERSITY

Blacksburg, Virginia 24061

MID-LIFE PLANNING FOR RETIREMENT

Letter 1

For ______________ and ______________

Tentative Retirement Date 19 ______

Dear Pre-retiree:

This series of letters is designed to guide you through the process of planning for retirement. Maybe you would like to put your name and the tentative date of retirement on the form above. This will make these letters your very own. You may also like to put them into a notebook or file folder. Planning for retirement takes place over a period of years and you may wish to refer back to some of the letters. You may also collect other information on retirement that could be kept with these letters.

These letters will contain information on the financial aspect of retirement such as: sources of income, cost to live, savings and investments, life insurance, property insurance, health insurance, estate planning, and possible ways to increase income.

The discussion on each of the subjects listed above is only an introduction. Additional sources of information will be listed throughout the series.

Merely reading the letters will be of little help. Put the information into action.

Retirement is a big event and the beginning of a new life experience. Those who have already retired emphatically state that a successful transition to retirement depends to a great extent on preparation.

This series should help you make wiser decisions concerning your retirement. It discusses alternatives for sources of income, how to live on retirement income, and steps you may need to take now.

Each letter of the series is only an introduction to a particular aspect of financial planning. Additional sources of information will be listed throughout the series. These sources will allow you to dig as deeply as you wish into the respective subjects. Digging deeper will take time, but this time can be some of the most valuable hours you can spend. Retirement is a big span of your life.

MHM: 146

The Virginia Cooperative Extension Service by law and purpose is dedicated to serve all people on an equal and nondiscriminatory basis. An Equal Opportunity/Affirmative Action Employer

An Educational Service of the Virginia Polytechnic Institute and State University, Virginia's Land-Grant University, with U. S. Department of Agriculture and Local Governments Cooperating

Retirement planning is very much like planning a trip. Any plan begins with establishing your destination, or goal, and a time table for taking each step toward the goal. The earlier you begin, the more choices you have.

For example - one part of a plan might look like this:

--Goal -- to retire in 15 years (1992)

--Time table -- 10 years before retirement, (1982) purchase a variable annuity.

At retirement, in 1992 cash in life insurance policiy and purchase a fixed annuity.

Your income, health, mental attitude, and use of time are all of utmost importance for successful retirement. An adequate income helps to support good health and a positive attitude and permits you to use your time as you wish.

WHAT RESOURCES DO YOU HAVE FOR RETIREMENT INCOME?

The most common sources for retirement income are pensions, social security, savings, investments and second jobs. Through your employer you may have health insurance, life insurance, or company stock plans that need to be incorporated into your retirement plans.

Pensions

Company pension plans come in a variety of forms. Employees of some companies pay a percentage of income into the company's plan. Some companies may pay the total cost, as an employee benefit. Whatever the method of payment, your pension is a valuable asset.

At any stage in employment you need to have some idea of what you can expect from your pension plan at any specific age.

Go to the person in your company who can best explain employee benefits to you. Do this now. If you are 2 years or less away from retirement go tomorrow. Have your list of questions written (include those on fringe benefits as discussed later in the series). Some of these pertinent questions are: What is the earliest date that you can retire? What is the latest? If there are penalities for early retirement, what are they? How much will the pension be? Exact figures will not be available, but you can get a rough estimate. When is the best date to retire? It may be to your advantage to retire December 31, Jan. 1, or July 1, etc. Do you get paid for unused sick leave or vacation time? Does unused sick leave count as length of service?

What options does the pension plan offer? Study these carefully. The plan may or may not offer you a choice of a lump sum, or monthly payments. Are you equipped emotionally or have experience to invest this large amount of money at one time for safety, adequate return on your investment and to provide your income for life? One way this could be done is through an annuity.

More than likely you won't have a choice and the pension is paid monthly, as an annuity.

There are some other options that are more common than the one just discussed. One option may provide income until your death and then no other payments will be made. Another option may provide a smaller income, but payments continue to a spouse after the employee's death.

Often people do not realize that there is a choice of options, or do not distinguish between the implications of choosing one option over another. This sometimes results in penalizing the retiree or the survivors. For example, if the option is chosen that the income increases at death of employee the surviving spouse may be left without income from this pension. Since most women outlive their husbands, the widows' financial situations should be given serious thought.

Many problems with pension plans arose before a law in 1974 brought them under closer study. The law does not require an employer to establish a pension plan, but it does set standards to which existing plans and those set up in the future must conform. It is in your own interest that you need to be familiar with the law as it pertains to coverage, vesting, financing and insurance.

The new law provides in general that:

- your company must cover all employees twenty-five years old and after one year of service with the company.

- vesting must be provided. Vesting is a guarantee right to some pension payment at age 65, depending on service. Should the employee leave the employment before 65, he can draw some payment (not full pensions) and not until 65.

- employees have a choice in vesting either

a. give the employee full rights after ten years service. Of course, service performed after ten years will be vested.

b. begin after 5 years service with vesting of 25 percent of pension credits, reaching 100 percent at the end of 15 years.

c. provide 50 percent vesting when the worker's age and years of service add up to 45 and build up to 100 percent vesting over the next five years.

It is important to understand these options and to be aware of how they would affect a job change, in specific years of your employment.

Pension plans may be financed by both the employer and employee. Some plans are financed only by the employer. When the employee pays into the plan, he pays income tax on his portion. For tax purposes, it is important to remember that when the employee collects his pension later, he does not pay taxes on this portion of the pension payments. This fact can be important in making some of your decisions pertaining to other investments. It may be economically sound to switch from some types of investment to other types during the years immediately after retirement.

The 1974 law provides insurance coverage of pension plans. The Pension Benefit Guaranty Corporation guarantees payment in case of failure or other termination of a pension plan.

Another aspect of the law is the transferability of a pension plan in a job-mobile society. Having a life-long pension coverage in private systems presents special problems, even with improved vesting. The Pension Reform Act encourages portability, but does not guarantee it. So, if you change jobs, give detailed attention to whether your present pension will be transferable, and if so, be sure records of your pension rights are transferred to your new employer.

Fringe benefits

The fringe benefits of employment are other important aspects of your financial planning for retirement.

Will your health insurance policies continue after retirement? If you will be eligible to participate, will your employer pay for these or will you pay the premiums? If you do have to pay for these you will need to shop around before your retirement date to compare other policies and costs. In case of health insurance, you will also want to buy new policies early enough to give you continuous coverage and that will cover periods of pre-existing conditions. For example, most policies have a waiting period of at least 6 months before it will cover an illness for which you have already received treatment.

There may be other fringe benefits. Under what conditions do these continue after retirement?

Company stock plans may be another fringe benefit and an investment that provides income for retirement. Some companies allow employees to purchase common stock of the employee's company at a reduced rate. If you are purchasing these now where will they fit into your financial plan for retirement? If your company offers this choice, should you participate to provide investments for retirement?

Social Security

Almost everyone will receive benefits from social security. Social security seems simple, but it is quite complicated when it comes to each individual situation. The amount one receives depends on age at retirement and average income for the years of "covered employment."

To receive maximum benefits from social security, one must wait until age 65 to retire. For a person who retires at age 62 (the minimum retirement age to draw Social Security) the benefits are reduced. Benefits that are begun at age 62 are 80 percent of the monthly amount that would be received if benefits began at 65. As it figures out, a person who starts drawing benefits at age 62 is generally ahead of the game for the first 15 years.

Before you qualify for benefits you must have received a certain number of "quarters of coverage." A quarter of coverage is any calender quarter (3-month period beginning January 1, April 1, July 1 or October 1) in which you are paid at least $50 in wages for work covered by Social Security.

The self-employed must have had at least $400 net earnings in a year to receive 4 quarters of coverage for that year. For persons beginning work since 1950, 40 quarters of coverage is required. For people employed before 1950, fewer quarters of coverage are required to receive benefits. For example:

If you reach age 62 in 1976 - 25 quarters needed, 1977 - 26, 1979 - 28, 1983 - 32, 1987 - 36, 1991 - 40.

Multiply the quarters by 4 if you would rather think in terms of years.

For help in planning your retirement and if you have changed jobs several times, you should check the official Social Security record of wages and self-employment income credit to you. Use post card form 7004, available at your Social Security office. It is important also to check records of the Social security office against your own record of earnings. Should there be a mistake, it must be reported within 3 years, 3 months, and 15 days.

The Social Security office also has a free folder, Estimating Your Social Security Retirement Check.

Social Security alone is not sufficient to support any American in dignity and comfort. It was never intended to be the only financial resource for retirement; however, it is an important part. When you have a close estimate of your individual benefits then you can better plan when to retire and how to best use your other resources.

When you approach retirement you will need to apply for Social Security Benefits. Benefits are not paid automatically. You may need to provide proof of the year of your birth, your marriage, and proof of age of dependant or children. If you do not have these, now is the time to get them.

Working married people are fully insured (eligible for Social Security benefits) at retirement and can draw benefits either in their own rights or as a spouse of a retired person. One should elect the coverage that provides the higher benefits.

There are some other special situations in which retirement benefits will be paid. For example, if husband is dependant on wife, if husband is deceased, or if a divorce was granted after 20 years and no remarriage. Every person's social security situation is unique. Again, check with the Social Security office for your coverage.

Pension Plans for the Self-employed and for Those Not Covered by Company Pension Plans

Keogh plans for the self-employed are highly advantageous for do-it-yourself retirement plans. These plans allow money to be invested for collection in retirement with deductions from current income for present tax purposes. The funds can be collected after age 59½ either in a lump sum or in installments at which time the money is taxable. After retirement, probably you will have a lower income and therefore be in a lower income tax bracket.

The Keogh funds can be in the form of a variety of investment media. The instruments can be certificates of deposit, mutual funds and others. Keogh plans can be set up at savings and loan associations, banks, or insurance companies.

A self-employed person who has one or more employees must also cover the employees.

A person who holds a job and also is self-employed may participate. The annual maximum amount that may be invested is 15 percent or up to $1,500.

Other Resources for Income

Retirement income can also come from savings and investments. If you are several years away from retirement, you may be in a position to accumulate some savings. A future letter will discuss savings and investments.

To repeat the opening sentence of this letter, next to employment and supporting a family, retirement is probably the biggest investment you will ever make. The purpose of this series is to motivate you to pursue further information.

In summary, there are sources of income for retirement through pensions for the employees and the self-employed. Certain fringe benefits need to receive attention as they are affected by retirement. Social security provides valuable resources for retirement income. The coverage we have now and the changes that occur--when we leave a job or when we retire--affect our financial situation. The important fact is that you know what you can expect as you plan for retirement. Keep in contact with your personnel or treasurer's office and the Social Security Administration.

The following references are recommended because they provide information on preparation for retirement, in addition to the financial aspect. If your city or county library does not have them, maybe they would purchase them. Most library personnel would like suggestions for new book purchases.

U.S. News and World Report, Money Management Library, Plan Your Retirement Now, Simon and Schuster, Order number 21853, 1976.

Collins, Thomas, The Complete Guide to Retirement, Prentice Hall, 1970.

Hunter, Woodrow W., Preparation for Retirement, Division of Gerantology, The University of Michigan, 1508 Rackham Building, Ann Arbor 48104, 1968, $3.00.

Buckley, Joseph C., The Retirement Handbook, Harper & Row, N.Y.

Ware, George W., The New Guide to Happy Retirement.

(Libraries may not want to purchase paper backs). Highly recommended and inexpensive for individuals to purchase.

Dynamic Maturity-monthly publication to members of Action for Independent Maturity, a Division of the American Association of Retired Persons.

Prepared by:

Hilda Dailey, Extension Specialist,
Home Management

Distributed by:

____
Extension Agent

The reference books were listed only for the purpose of information and the VPI & SU extension service does not recommend any one of the reference books to the exclusion of others which might be available.

Issued in furtherance of Cooperative Extension work, Acts of May 8 and June 30, 1914, in cooperation with the U.S. Department of Agriculture. W. R. Van Dresser, Dean, Extension Division, Cooperative Extension Service, Virginia Polytechnic Institute and State University, Blacksburg, Virginia 24061.

COOPERATIVE EXTENSION SERVICE
U.S. DEPARTMENT OF AGRICULTURE
Virginia Polytechnic Institute
and State University
Blacksburg, Virginia 24061