

## Retirement plans present many changes

Money Manager/by Karin Price Mueller – [www.businessstoday.com](http://www.businessstoday.com)

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### Problem:

Vinny and Leila are tired of working for other people. After decades of slaving to pay the bills, the couple is hoping for a different life in retirement. The couple, whose names have been changed for publication, came to the Herald to see whether they could reach that goal in 18 months, when Vinny turns 56 and Leila turns 55.

“I'd like to have a lot of leisure in retirement but I feel awfully guilty working two jobs for so long, I've never given into the community,” says Vinny, who works as an insurance underwriter and a medical records supervisor. He earns \$92,200 a year between the two jobs.

He and Leila, who earns \$6,500 a year working part-time as a bank teller, would like to spend a lot of their retirement volunteering.

They'd also like to become snowbirds - spending about eight months of the year at their North Shore home and the rest of their time in Florida.

Vinny and Leila own a one-bedroom condo in Florida, mortgage-free, but they're interested in upgrading to a two-bedroom unit in the same development. They hope the larger condo will offer more space should any of their three grown daughters visit with their families. They say they can sell their current unit for \$165,000, but the larger one will cost about \$205,000. They'd like to pay cash for the difference so they can stay mortgage-free.

They hope their retirement assets, which could soon reach the \$1 million mark, would cover their other expenses.

Vinny contributes 6 percent of his salary to the 401(k) offered by his insurance job, and his employer matches 3 percent. The account, worth \$529,245, is invested in Stable Value Fund, Dreyfus Lifetime Portfolios: Growth, Fred Alger Growth, Dreyfus Emerging Leaders and Templeton Foreign Fund. Vinny also expects to receive a pension worth \$29,244 a year upon retirement.

Vinny also has some money growing in three other plans from former employers. The accounts spread the \$213,000 in assets across funds including Fidelity Select Electronics, Fidelity Magellan, CREF Stock and CREF Global Equities.

Vinny also has an individual retirement account with Legg Mason, valued at \$38,210. The account is invested in funds, such as Legg Mason Value Trust and Van Kampen Emerging Growth, and stocks, including Photoelectron Corp and State Street Corp.

Leila's IRA, also with Legg Mason, is worth \$21,782. The account is invested in stocks, including Worldcom and Wal-Mart, and such funds as Van Kampen Emerging Growth.

The couple also has a non-qualified joint account, held at Legg Mason, worth \$85,598. The account is invested in such stocks as Public Storage Inc., General Electric and AOL/Time Warner. They also hold corporate bonds issued by Global Crossings and funds including AIM Weingarten Fund.

Vinny hasn't been happy with the performance of the joint account, which he moved to a brokerage house just before the market's downturn. He had made his own investment decisions and was happy with his returns, but he took more risk with the broker and that's when the market headed south.

“They made it very easy to consolidate accounts,” Vinny says. “But in retrospect, with the fees and the downturn, I got lazy and we got hit over the head.”

So the couple is looking for some advice about where their investments will do the most good for them between now and retirement, and beyond.

In cash savings, they have \$75,000 in a credit union, \$5,000 in a savings account and \$2,500 in a checking account.

The couple has also saved \$14,000 in EE Savings Bonds to help a daughter pay for her wedding - as they did for their other two daughters. The girls are no longer financially dependent upon them, but Vinny and Leila try to help the girls whenever they can.

"We tend to be a little more generous with our family than we should," he says. "But that's OK because it makes me feel good."

### **Solution:**

#### **Tweaking cash flow should let snowbird wannabes volunteer**

Vinny and Leila can reach their goals, but it will take a little reconfiguring of their portfolio to give them enough cash flow in the first couple of years.

"They've saved a good amount for retirement and their cost of living is very reasonable," says **Linda Homsey**, a certified financial planner with Freya Financial Services, of Wakefield. "The problem is the six years between retirement and when they start to receive Social Security."

Vinny and Leila estimate their expenses in retirement will be about \$56,000 a year. When they retire, they'll receive Vinny's annual pension of \$29,244, but that leaves a shortfall of \$26,756 per year.

Homsey says the couple's non-qualified assets would cover that shortfall until they receive Social Security and are able to dip into their 401(k)s and IRAs. But this is where the couple has to make their first choice.

If they don't buy the larger condo, they can afford to fund the shortfall solely from money in their non-qualified accounts. But if they're planning to use their \$75,000 credit union account to pay cash for the larger condo in Florida, they'll have to dip into their retirement accounts two years earlier - something they can do when they reach the 59 age requirement.

But before they can touch those funds without penalty, they'll have to use money from the non-qualified brokerage account to pay for the income shortfall. They have enough money there, but the problem is the account is filled with inappropriate, risky investments.

"That account is all in equities," Homsey says. "If they're going to be drawing on that for his income in a year-and-a-half, it's a much too aggressive portfolio."

If the goal is to use money in less than five years, Homsey says it should be in relatively conservative investments. She recommends the couple reallocate the funds in that account to income-producing investments, such as short- or intermediate-term bond funds or money market funds. But before selling anything in that account, she suggests the couple examine their cost basis to determine tax implications.

Next, Homsey recommends Vinny and Leila take a look at their qualified investments.

"My biggest concern for them is just to reevaluate their investment strategy," she says. "They need to think about their goals and make sure their investments fit with their true risk level."

Because the couple has a life expectancy of about 35 years after retirement, they need to have substantial growth in their portfolio. She says their allocation of 79 percent stocks, 15 percent bonds and 6 percent cash is reasonable, but she takes issue with a few of their specific investments.

“I want to make sure they're comfortable with the risk they're taking and they know what they're getting into,” she says.

For example, in one of Vinny's 403(b) plans is a stake in Pilgrim Internet Fund, which lands in the bottom 98 percent of funds, according to Morningstar.

If Vinny and Leila want to remain in an Internet fund, she recommends they consider Kinetics Internet Fund, which has a longer track record. And if they stick with risky actively managed funds, Homsey suggests the couple balance the risk with a passive index fund that mirrors the Standard & Poor's 500 or the Wilshire 5000.

Another change should be with the AIM Weingarten Fund, which is in the couple's taxable account. The fund hasn't performed as well as its peers in recent years, Homsey says. She recommends the couple instead reposition the money into a bond fund or money market account as they will probably draw on the money in a couple of years.

Also in the couple's taxable account is Van Kampen Emerging Growth. The fund ranks in the top 3 percent of its category for the most recent three-year period, and in the top 10 percent over the most recent five-year period. But because the fund has a deferred load for five years, if the couple sells those shares too soon, they'll have to pay a fee. Homsey recommends they wait until the load drops before selling.

Vinny and Leila also need to make some estate-planning moves. Homsey says the couple should consider setting up credit shelter trusts, which will allow them to make the most of their unified credit. Because most of the assets are in Vinny's name, they could run into tax trouble down the road. An estate-planning attorney would be a good investment for the couple at this time, Homsey says.

“Assets can pass from one spouse to another with no estate tax repercussions,” she says. “But when the second spouse dies owning all the assets it's the surviving family that loses out.”