

# Financing Your Retirement Future

December 2007

## When Will You Retire?

Here are some issues you should consider before making the important financial decision of when to retire.

### Is your nest egg adequate?

It's obvious, but the earlier you retire, the less time you'll have to save, and the more years you'll be living off of your retirement savings.

For example, if you retire at age 65 instead of age 55, and save an additional \$20,000 per year at an 8% rate of return, you can potentially add \$312,909 to your retirement fund. (This is a hypothetical example and is not intended to reflect the actual performance of any specific investment.) The average American can expect to live past age 77. (Source: National Center for Health Statistics) With future medical breakthroughs likely, it's not unreasonable to assume that life expectancy will continue to increase. Is your nest egg large enough to fund 20 or more years of retirement?

### IRAs and employer retirement plans

The longer you delay retirement, the longer you can build up tax-deferred funds in your IRAs or employer-sponsored retirement plans. If your employer has a traditional pension plan, leaving the company before normal retirement age may greatly reduce the final payout you receive from the plan.



You could also pay a price for retiring early if you participate in a 401(k) plan. You could end up forfeiting employer contributions in which you're not yet fully vested. You would also miss out on the opportunity to make additional contributions to the plan, and participate in future employer contributions.

### Health insurance

Keep in mind that Medicare generally doesn't start until you're 65. Does your employer provide post-retirement medical benefits? Are you eligible for the coverage if you retire early? If not, you may have to look into COBRA or a private individual policy--which could be an expensive proposition.

### Social Security benefits

You can begin receiving your Social Security retirement benefit as early as age 62.

However, your benefit may be 20% to 30% less than if you waited until full retirement age (65 to 67, depending on the year you were born). And if you continue to work past age 62, your benefit will generally be reduced \$1 for each \$2 you earn above the annual earnings limit (\$12,960 in 2007) until the year you reach full retirement age.



In some cases it may be to your advantage to delay receiving your Social Security retirement benefit even after you reach full retirement age. If you do so, your Social Security benefits may increase for two reasons. First, each additional year that you work adds another year of earnings to your Social Security earnings record, resulting in potentially higher retirement benefits. Second, under the Social Security Administration's delayed retirement credit, your benefit will increase by a certain percentage for each month that you delay retirement up to age 70. The percentage increase varies, depending on the year you were born.

### Is phasing into retirement right for you?

Retirement need not be an all-or-nothing affair. If you're not quite ready, financially or psychologically, for full retirement, consider downshifting from full-time to part-time employment. This will allow you to retain a source of income and remain active and productive.

Some employers are adopting "phased retirement" programs to help retain employees who might otherwise retire early, begin receiving their pension benefits, and then seek employment elsewhere, often with a competitor. Phased retirement usually refers to an arrangement that allows employees who've reached retirement age to begin receiving their pension benefit while continuing to work for the same employer with a reduced work schedule or workload.

You benefit from the opportunity to continue active employment at a level that allows you greater flexibility and time away from work, smoothing the transition from full-time employment to retirement. And your employer benefits by retaining the services of an experienced worker. Ask your plan administrator if phased retirement is an option under your employer's pension plan.

## Money for Your Life: Determining Your Life Insurance Need

Life is priceless. But if you're purchasing life insurance, a financial value needs to be assigned to it. How do you determine how much your life is worth in dollars to the family you'll leave behind?

### The thumb no longer rules

There are several rules of thumb you might have heard about when it comes to calculating your basic life insurance coverage need. Figure six to eight times your annual gross income, and maybe throw in special funding needs (e.g., college for the kids) on top of that. Or back into your answer by determining your premium expense as a percentage of your income--6%, plus an additional 1% for every dependent--and buy as much insurance as you can for that amount.

These rules of thumb are simple enough to use. Trouble is, they don't take into consideration your individual circumstances. Consider them no more than a rough starting point.

### Are you what you earn?

The human life value approach, often used in court cases involving wrongful death suits, attempts to measure your economic worth to those who would be affected by your death. Your human life value is defined as the present value of your future net earnings (adjusted for inflation) that would be used for your family's benefit, plus the value of other services you contribute (e.g., you mow the lawn rather than pay to have it done), through your planned retirement age. The resulting figure represents the amount of life insurance coverage you should have to adequately replace your economic value to your family should you die today.

While the human life value approach is more precise than any of the rules of thumb, it still has its weak points. In one sense, it tends to overstate your family's insurance need by failing to account for other assets and sources of income that can help support your family if you die. In another sense, it tends to understate your family's life insurance need by failing to account for certain large lump-sum expenses that will come up only after you die-- for example, final medical expenses, funeral costs, and estate settlement expenses. Finally, by focusing primarily on replacing your income, this approach may ignore the financial needs of your surviving family members.



### It's all in the family

One of the more comprehensive methods of calculating your life insurance need is the family needs approach, which assumes that the purpose of life insurance is to cover the needs of your surviving family members. Accordingly, it focuses primarily on estimating what their immediate and ongoing financial needs would be upon your death.

Your family's immediate financial need will require cash to cover expenses incurred upon your death, such as final medical and funeral expenses. Their ongoing financial need will require an income stream to meet family expenses associated with different situations that will last until your surviving spouse's death (e.g., child dependency, college, spousal income needs until retirement, and spousal retirement). These needs will vary depending on your spouse's and children's ages, whether any family member has special needs, your spouse's capacity to earn income, your spouse's intended retirement age, and his or her life expectancy.

Under the family needs approach, the amount of life insurance you'll need will equal your family's immediate need plus the present value (after other expected sources of income are deducted) of your family's ongoing need, less the value of other assets that could meet some of these needs.

The general equation would look like this:

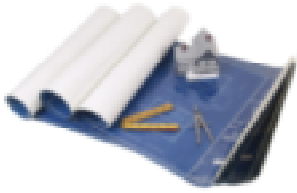
$$(Im + P[On - Xi]) - As = LIN$$

where **Im** equals the **I**mmEDIATE financial need at your death, **P[On - Xi]** equals the **P**resent value of your family's **O**ngoing financial need less other **eX**pected income, and **As** equals the value of existing **A**ssets available to defray some of these expenses. The result is your **L**ife **I**nsurance **N**eed.

By examining in detail your family's anticipated expenses during various periods after your death, the family needs approach provides a realistic estimate of your life insurance need. Not only does this approach offer more accurate estimates than the various rules of thumb, but it may also provide a clearer estimate of your family's needs than the human life value approach.



# Modifying a Home for Independent Living



Because many homes aren't designed to accommodate changing physical needs, it's sometimes challenging for people with disabilities to live independently. But fortunately,

homes can be modified to remove barriers to independence and reduce reliance on caregivers. For older individuals, home modifications can delay or even prevent the need for costly care in a nursing home or assisted-living facility.

Improvement options will depend on individual needs and physical concerns. But here's a broad look at some of the home modifications that might help make day-to-day living safer and easier for you or a loved one.

## Inside the home

### Kitchen

- Remove cabinet doors to make it easier to see and reach items
- Use turntables inside cabinets to reach supplies easily
- Lower countertop surfaces and kitchen cabinets to make them more accessible
- Install a cook top and a low wall oven instead of using a range; install an adjustable mirror over the stove to make viewing cook top from a wheelchair easier

### Bathroom

- Install a raised toilet with attached handrails (portable seats are also available if replacing the toilet is impractical)
- Cover sink handles with rubber grips to make it easier to turn the water on and off
- Install grab bars or poles near the toilet and shower
- Replace bathtub with low-threshold shower

### Other living areas

- Replace door knobs with lever-style handles, or install door knob covers that are easier to grip and turn
- Add nightlights to prevent nighttime falls
- Remove throw rugs and thick doormats; replace padded carpet with thinner, level-loop carpet to prevent tripping and facilitate wheelchair or walker navigation
- Widen doorways, remove doors, or install special hinges that allow doors to open wider
- Install a ceiling lift device that will allow independent movement around the home
- Install a stair lift or an in-home elevator

## Outside the home

- Apply nonskid surfaces to garage floors, decks, stairs, and walkways
- Install handrails on both sides of stairs

- Replace standard exterior lights with motion-sensitive or photo-sensitive lights
- Construct an entrance/exit ramp

### **Daily living aids and assistive devices**

*People often don't realize how many products are available to help people maintain their independence. Here are just a few that can be found at pharmacies and medical equipment suppliers:*

- Amplified phones
- Large button remote controls
- Lift chairs
- Shower or tub chairs
- Reachers that grasp hard-to-pick-up items
- Optical magnifiers that project text onto a TV screen
- Personal emergency response systems

### **Paying for home modifications**

Many home modifications are simple and inexpensive, but if you need to remodel extensively or hire a contractor, you may need help paying for improvements. Fortunately, financial help is available from public and private agencies and charities. For example, states and communities may offer special financing or grant programs, and charities often organize repair or improvement projects. To find help available in your community, contact your local Area Agency on Aging through the nationwide Eldercare Locator at (800) 677-1116, or through their website, [www.eldercare.gov](http://www.eldercare.gov).

### **Tax breaks**

If you itemize deductions on your federal income tax return, you may be able to deduct home improvements that are primarily for medical care and prescribed by your doctor. However, you can deduct only the amount that is

more than 7.5% of your adjusted gross income. For example, if your adjusted gross income is \$70,000, then you would be able to deduct expenses that exceed \$5,250. Expenses that generally qualify include the cost of installing ramps, lowering or modifying cabinets, and adding grab bars. If an improvement increases the value of your home, it may be only partially deductible. For more information and a list of deductible expenses, see IRS Publication 502, Medical and Dental Expenses.

Some states also offer tax breaks to their residents, including sales tax exemptions, deductions, or tax credits; local property tax credits or abatements may be available as well. For more information, talk to a tax professional.

- Modifying a Home for Independent Living

Life Insurance Need

- Money for Your Life: Determining Your

- When Will You Retire?

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