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## By the numbers<sup>1</sup>

- **3.3** is the number of workers for each Social Security beneficiary today. By 2032, there will be 2.1 workers for each beneficiary.
- **41%** of the income of the elderly is received from Social Security benefits.
- **82.5** years is the life expectancy of a 65-year-old. In 1935, the life expectancy of a 65-year-old was 77.5 years.

<sup>1</sup> Social Security Administration, 2007

# 10 rules for the retirement road

Many investment professionals recommend that investors follow these 10 strategies as they plot their way toward retirement. If you are worried that your retirement investment plan is adrift, these rules could help you steer in the right direction.

## Rule 1: Pay yourself first.

Many investment professionals start their preretirement pep talk with the same three words: “Pay yourself first.” This includes contributing the maximum amount possible to your 401(k) plans and investing additional amounts in IRAs and mutual funds through automatic payroll deductions. Automatic investment plans are an easy way to stick with a retirement investing program because the money is invested before it can get spent on anything else. While automatic investing does not guarantee a profit or protect against a loss in declining markets, it does make retirement investing a priority. With any automatic investing program you should, of course, consider your financial ability to continue to invest through periods of low prices.

## Rule 2: Don't let today's bills sink tomorrow's needs.

Supporting yourself and your family is not easy. Chances are, especially if you have children, your household expenses will grow over time. That's why it's important, especially through times of difficulty and new expenses, to keep contributing toward your retirement.

When you are thinking of reducing or ceasing investing for your future to cover current expenses, stop, think, and try to find another way to cover your current expenses.

## Rule 3: Put time on your side.

It's simple. When you give your money more time to accumulate, the potential earnings on your investments — and the annual compounding of those earnings — can make a big difference in your final return.

*(continued on page 2)*

## Key points

Today is the best time to start planning for retirement. Why?

- Time is an investor's greatest asset.
- Once you have a plan in place, it is easy to modify.
- Investing is a habit that is best started as soon as possible.
- Your retirement is ultimately your responsibility.



(continued from page 1)

Consider a hypothetical investor who saved \$2,000 per year for 10 years, then didn't add to her nest egg for the next 10 years.<sup>2</sup> She has \$50,042 after 20 years, assuming she earned 6% annually in a tax-deferred account. Another hypothetical investor waited 10 years, then tried to make up for lost time by investing \$3,000 annually for the next 10 years. Even though he invests more — \$30,000 versus the early bird's \$20,000 — he still ends up with a smaller nest egg. Assuming he also earns 6% per year, his final account value is only \$41,915. Most of the procrastinator's nest egg — 72% — is the principal he invested. The majority of the early bird's account — 60% — is earnings.

#### Rule 4: Don't count on Social Security.

While we keep hearing that Social Security isn't going anywhere, it's still very likely, especially if you are under age 50, that the program will be very different from its current form when you retire.

According to the Social Security Administration, Social Security benefits represent 41% of the income of the elderly.<sup>3</sup> They also state that by 2032, there will be many more elderly Americans than there are today, growing to 72 million from 38 million.<sup>3</sup> While the dollars and cents result of this growth is hard to determine, it is clear that investing for retirement is a prudent course of action.

<sup>2</sup> This hypothetical example is for illustrative purposes only and is not intended to represent future performance of any MFS product. Investment return and principal value will fluctuate, so your investment may be worth more or less than the original value.

<sup>3</sup> Social Security Administration, August 30, 2007

#### Rule 5: Resist borrowing from your 401(k).

Loans are a popular feature of 401(k) plans. People like being able to get access to their money. But many investment professionals recommend clients consider borrowing from other sources, such as the equity in one's home, before taking a 401(k) loan.

Here are some reasons why.

**Fixed return.** When you pay yourself interest when you pay back a 401(k) loan, your interest rate is the amount you earn on that money. This may be a modest return compared with what your money could earn if you left it invested in the financial markets.

**Payback challenge.** Repaying a 401(k) loan when trying to maintain contributions may be difficult. There is a real chance that your retirement plans may suffer when you try to repay and continue to invest simultaneously.

**Tax penalties.** Switching jobs before a 401(k) loan is repaid can bring unwanted tax consequences. You may be able to pay off or transfer your loan to your new employer's plan, but if neither option is available to you, your loan balance will be considered a distribution from your plan. As a result, you may owe ordinary income taxes and a premature distribution penalty tax of 10% unless you meet one of the age or systematic payout method exemptions provided in the Internal Revenue Code.

**Double taxation.** The money you use to pay interest on your loan will be taxed twice. It will be taxed first when

you are repaying the loan because, even though you can contribute to a 401(k) with "pretax" dollars, you can't do the same with loan payments. It will be taxed a second time, as other 401(k) earnings are, when you make withdrawals from your account in retirement.

#### Rule 6: Don't "cash out" retirement plans when switching jobs.

When you leave a job, the vested benefits in your retirement plans are an enticing source of money. It may be difficult to resist the urge to take that money as cash, particularly if retirement is many years away. But generally you will have to pay federal income taxes, state income taxes, and a 10% penalty if you're under age 55. This can cut into your investments significantly. If the state income tax is 7.5%, for example, someone in the 25% federal tax bracket would lose 42.5% of the amount he or she took.

$$\begin{array}{r}
 25.0\% \text{ (federal tax)} \\
 + 7.5\% \text{ (state tax)} \\
 + 10.0\% \text{ (penalty)} \\
 \hline
 = 42.5\% \text{ (total tax and penalty)}
 \end{array}$$

When changing jobs, you generally have three options for leaving your retirement money invested. You can keep the money in your old employer's plan, roll it over into an IRA, or transfer the money to your new employer's plan, if that plan accepts rollovers. Ask your advisor about these three options before deciding which will work best for you.

(continued on page 3)



(continued from page 3)

**Rule 7: Take advantage of your IRA options.**

The Roth IRA has become a popular way to expand retirement investing for many investors. But with many IRA options available today, it’s important to know why you are investing before you decide where to start. And, once you decide on a direction, it’s important to make your annual contribution. Annual contribution limits recently have increased, making IRAs a more valuable way to invest for retirement. Individuals over age 50 can make additional “catch-up” contributions each year. Your investment professional can help you determine which IRA could work best for your situation.

**Rule 8: Compare the merits of the Roth IRA and a 401(k) plan.**

The variety of retirement savings options available today is a boon for investors. But the range of choices can also be confusing. Many investors try to compare the potential advantages of the Roth IRA with their 401(k) or other type of defined contribution plan at work. The choice is especially difficult for those with limited budgets who can afford to invest in only one of the options. Work with your investment professional to determine whether the Roth IRA or your 401(k) offers more advantages for you. The answer will depend on many factors, including how many years you have left until retirement, your tax bracket, and whether your employer matches contributions to your 401(k).

**Rule 9: Don’t try to time the stock market.**

Some investors, even those for whom retirement is still many years away, frequently shift their money in and out of the stock market. They’ll get out when they fear a crash and get back in when they expect a boom. The problem with trying to time the market is that no one can consistently predict the short-term events that push the market up or down. It may be better to consider an investing plan adjusted for your goals, time frame, and risk tolerance that diversifies your investments, allocates them among different asset classes, and rebalances your portfolio.

**Rule 10: Allocate, diversify, and rebalance**

You have certain long-term financial goals in mind. You also have a certain tolerance for risk when it comes to investing your money. Asset allocation can help you find and maintain your balancing point. So you can pursue your goals at a risk level you find comfortable.

As part of a **disciplined diversification**<sup>SM</sup> investment strategy, asset allocation enables you to seamlessly follow this proven three-step process.

**Allocate** your assets across the major asset classes — stocks, bonds, and cash — to help you pursue the optimal returns for the risk level you’re willing to undertake.

**Diversify** within each class to take advantage of different investment styles — such as growth and value stocks — and various market sectors — such as government and corporate bonds.

**Rebalance** regularly. Market activity can shift the percentages of your portfolio that you have dedicated to each asset class. Rebalancing will help you maintain your desired allocation.

**Additional MFS resources**

“Retirement calculators” in the Retirement Planning Section on [mfs.com](http://mfs.com)

**For more information, contact your investment professional or visit [mfs.com](http://mfs.com).**

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