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What Will $2 Million Get You In Your Retirement?

People often ask how much money they will need to meet their retirement goals. But let's turn this common question on its head: What will $2 million actually get you in retirement? This is an interesting query because (a) many people believe that $2 million is a comfortable amount to meet their retirement goals and (b) it allows us to examine the different ways in which a hypothetical couple can use $2 million without running out of money.

As with any retirement calculation, this one involves numerous assumptions. Nevertheless, as long as the assumptions are reasonable—for example, using 6% for equity returns rather than the 10% figure that many illustrations often include—it's possible to arrive at a conservative estimate of how much money you might need to retire comfortably.

Let's start with these assumptions for our hypothetical couple:

Before generating a retirement plan for this couple, it's important to clarify what constitutes "success" in this situation. Because we live in a dynamic world, especially when it comes to investing, we'll look at this question in terms of probability, using something known as a Monte Carlo analysis, which factors in thousands of scenarios with widely varying assumptions and investment returns in every year. For purposes of this example, we'll define success as a probability of at least 85% that the couple's funds won't run out during their retirement.

Using our assumptions for this hypothetical couple, the Monte Carlo analysis shows a 97% probability that they won't exhaust their savings. That easily meets our definition of success and suggests that they might be able to spend more than $70,000 a year and still succeed, based on the 85% threshold.

So, how much can this couple

Inflation (CPI)	3.00%
Current Age of Both People	65
Age at Retirement	65
Age When Both People Have Passed Away	95
Social Security at Age 67 (combined)	$35,000 per year
Average Savings Rate	None (Already Retired)
Total Investment Balance Today	$2 million (50% in Taxable, 50% in IRAs)
Recurring Annual Expenses in Retirement	$70,000
Investment Mix Before Retirement	70% U.S. Value Stocks, 30% Medium-Term Treasuries
Return Assumption Value Stocks	6% per year
Standard Deviation Value Stocks	16.20%
Return Assumption Treasuries	1.5% per year
Standard Deviation Treasuries	7.20%

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Here's A Fast And Easy Way You Can Supplement A Will

Do you want to provide guidance above and beyond the terms of your will? You can use "letters of instructions" to fill the gaps. Although such documents aren't legally binding, they still can be helpful. Here are several issues you might address in this way:

- A letter could detail an inventory of your assets, including checking and savings accounts; safe deposit boxes; retirement plans; Social Security and VA benefits; stocks, bonds, and other investments; real estate holdings; and life insurance and other insurance policies.
- It also could specify where important papers are located—for example, disclosing where your income tax returns and credit card information may be found. This can ease matters for your executor.
- It also might address other personal matters, including funeral, burial, or cremation arrangements; addresses and telephone numbers of people and organizations to be notified when you die; and other specific instructions (for example, providing holiday gifts to caretakers).
- Finally, you could use a letter of instruction to indicate personal preferences, such as your wishes regarding a child's education. You also might explain the bequest each heir will receive and the reason for the choice.

Letters of instructions are meant to supplement, not replace, a valid will. Nevertheless, they can offer valuable guidance at a time of need.

Robert Pyle

Why Roth IRAs Are Still Red-Hot

What's the next big thing in financial planning? It's actually something that has been around for years: the Roth IRA. This tax-advantaged account offers the promise of future benefits without some of the restrictions that hamper traditional IRAs.

What makes a Roth so special? With a Roth IRA that's at least five years old, most distributions after you've reached age 59½ are completely tax-free, while earlier payouts may be wholly or partially tax-free under the tax law's "ordering rules" that treat the first money out of the account as coming from your contributions, which aren't taxable. Also, you never have to take the "required minimum distributions" (RMDs) that force you to deplete a traditional IRA. Those RMDs and other distributions are taxable at ordinary income rates (except for any portion representing nondeductible contributions) reaching up to 39.6%. RMDs for IRAs become mandatory after age 70 ½.

There are two main ways to establish a Roth and take advantage of its benefits: through annual contributions or with a conversion from a traditional IRA.

1. Annual contributions. You can set up a Roth IRA and make contributions each year of as much as $5,500 ($6,500 if you're age 50 or over). But the ability to contribute to a Roth is phased o utat higher-income levels.

2. Roth conversion. Anyone can convert a traditional IRA to a Roth, or use a conversion to add to a Roth you've already established. In either case, you must pay tax at ordinary income tax rates on the taxable portion of the converted funds. Advance planning can help you minimize the tax damage.

One popular technique is to convert just enough to fill up extra "space" in the lower tax brackets while triggering as little tax as possible in the top tax brackets. This can be particularly powerful if you expect to be in a higher tax bracket in retirement than you are in now.

Suppose you're married and file a joint tax return, you have $500,000 in a traditional IRA, and your adjusted gross income in 2014 is $130,000. Using current tax rates, you are in the 25% tax bracket, but you anticipate being in the 35% bracket during retirement. If you fill up the 25% tax bracket (which tops out at $148,850) by converting $18,850 in traditional IRA funds to a Roth, you'll save 10% in tax (the difference in the current 25% rate and the future 35% rate). Assuming you repeat this strategy over several years, the savings could be as high as $50,000 (10% of $500,000).

This assumes you can pay the conversion tax with funds from outside the IRA, which might be a problem. Other factors also may come into play. So be sure that converting to a Roth IRA in this way makes sense for your situation before you take the plunge. Roth IRAs are hot, but you don't want to get burned. ●

Fill Up Tax Brackets To The Brim

Remember the days before self-service when you could drive your car to a gas pump and tell the attendant to "fill 'er up"? There are good reasons to take the same approach to selling securities before the end of the year. If you're careful to fill up your lower tax brackets with long-term capital gains, you can pocket some cash and pay little, if anything, in federal income tax.

Before you start filling up tax brackets, it's important to understand the basic tax rules affecting capital gains.

Currently, there are six federal income tax brackets ranging from 10% to 39.6%. Most "ordinary income," as well as short-term capital gains from sales of assets you hold a year or less, is taxed under this graduated rate structure. But long-term capital gains from selling securities you've owned longer than a year may be taxed at three capital gain rates:

- The 0% rate applies to long-term capital gains of investors in the two lowest brackets (10% and 15%).
- The 15% rate applies to long-term gains of those in the middle three brackets (25%, 28%, and 35%).
- The 20% rate applies to long-term gains of investors in the top bracket (39.6%).

With the tax system's graduated rate structure, even investors whose capital gains eventually will push them into the 39.6% tax bracket may be able to benefit from having part of their capital gains taxed at the lower 0% and 15% rates. That's what tax bracket management is all about.

The best way to explain the concept of filling up tax brackets with long-term gains may be with an example.

Hypothetical facts: Suppose that 2014 will be a low-income year for you because of losses from your S corporation or other business circumstances. Not including your

Dispel These 7 Popular Myths About Retirement

Retirement is changing. People are living longer, and many stay healthy and vital into their 80s and 90s. Working, at least part time, has become more commonplace. Yet with fewer and fewer corporate pensions to fall back on these days, the money to pay for a long life after work may not be there. And with change comes confusion and misperceptions about what really may happen during your retirement, however you define it.

Consider these seven common ideas that may prove overly optimistic—and then tweak your plans to make sure you don't fall short of your goals:

Myth #1: You'll have saved enough for retirement when you get there.

According to a 2014 survey by the Employee Benefits Research Institute (EBRI), an independent research firm, only 42% of current workers over age 55 say they've saved at least $100,000, while just 23% have set aside more than $250,000. The EBRI survey also indicated that just 18% of all workers were "very confident" they've saved enough for retirement. You easily could find yourself facing a shortfall.

Myth #2. You'll spend a lot less than you do now.

Some cash outlays, such as paying off the mortgage and sending the kids to college, no longer may apply. But what do you want your retirement to look like? If you've envisioned globe-trotting or indulging in expensive hobbies, you may find that will erode your nest egg more quickly than you expected. Unexpected expenses—high-priced dental work, say, or a down payment for a child's home—also can siphon away funds.

Myth #3. You'll save a lot of money when you downsize your home.

Moving to a smaller place probably will reduce maintenance costs and property taxes. But that doesn't mean you won't still have all the usual expenses associated with home ownership—just on a smaller scale—plus other possible fees that may apply if you've moved into an over-55 community. And if you've relocated to a ritzy neighborhood in a city or resort area, your expenses could go up.

Myth #4. You'll continue working past the normal retirement age.

You may want to stay on the job or shift to something else, but such plans don't always work out, and health problems also could pose obstacles. And if you're counting on job income to shore up your finances through many years of "retirement," not being able to do it—or deciding you're just not up to it—could leave a big hole in your retirement income.

Myth #5. You easily can get a part-time job if you need one.

When you retire from your full-time position, you might seek part-time employment, but those jobs may be harder to find, and to keep, than you imagine. You may be competing with youngsters who are more tech-savvy than you for jobs requiring computer skills. What's more, if you're living in an area with numerous other retirees, which is often the case, the competition can be fierce.

Myth #6. You can rely on Medicare for all your medical expenses.

Retirees often expect Medicare to pick up the entire cost of physician visits, hearing or eye exams, or the like, but that's simply not how the system works. In fact, Medicare covers only roughly half of such expenses, according to data recently provided by the Kaiser Family Foundation. And don't overlook the exorbitant costs of staying in a long-term care facility or paying for in-home nursing care. If you don't have a supplemental policy, Medicare might not provide enough coverage for you.

Myth #7. You can rely on Social Security for most of your income.

Different people have different ideas about Social Security. Some almost disregard those payments from the government, thinking they'll be too small to make any difference in funding retirement. Others, though, talk about Social Security like it's the be-all, end-all. It's neither. The fact is, Social Security can be genuinely helpful, often covering some of your essential expenses. But for most people it's not nearly enough to live on. The Social Security Administration says the average monthly benefit in 2014 is $1,294, which works out to $15,528 a year. That's why it's vital to take steps to supplement Social Security with income from investments, employer retirement plans, IRAs, and other sources.

There's one more myth we would like to expose—that it's too late to change your destiny. Reexamine your basic assumptions about your retirement and then make a reasonable retirement savings plan based on your needs and realistic objectives. ●

investment income, your taxable income on a joint federal return should be only $50,000, but the upper threshold of the 15% bracket is $73,800. That leaves room for another $23,800 of income ($73,800 - $50,000) before you reach the 25% bracket—and the 15% bracket for long-term capital gains. So if you pull down a $23,800 long-term gain before year-end, the entire amount will be taxed at the 0% rate.

What's more, consider that the upper threshold for the 35% rate is $457,600. Any other long-term gains below that threshold will be taxed at the 15% rate.

Of course, there are other factors to consider, including the 3.8% surtax on net investment income. Also, be aware that capital losses offset capital gains plus up to $3,000 of annual ordinary income. But the long and the short of it all is: You can manage your tax brackets to maximize favorable tax rates for long-term capital gains. ●

Are You Confident About Retirement?

Every year, the Employee Benefits Research Institute (EBRI), an independent research firm, gauges the confidence levels of retirement-savers. The results of its 24th Retirement Confidence Survey may make you sit up and take notice.

What jumps out is that an astounding 36% of current workers say they have saved $1,000 or less for retirement. Naturally, this figure is skewed somewhat by younger employees, of whom about half have less than $1,000 in savings, but 24% of the respondents over age 55 still haven't scaled the four-figure mark. At the same time, 42% of workers over age 55 say they've saved at least $100,000, while 23% in that age category have socked away more than $250,000.

As far as the rest of the report goes, Americans are becoming slightly more confident about retirement saving, although there's still plenty of cause for concern.

According to the 2014 survey, based on interviews with 1,000 current workers and 500 retirees, 18% of the current workers were "very confident" they would have enough money to live on comfortably throughout their retirement. That's up from a record low of 13% lasting from 2009 through 2013. Among retirees, the "very confident" figure was 28%, higher than the 18% figure last year.

Significantly, EBRI noted that the numbers haven't bounced back all the way since the downturn year of 2008. In that watershed year, 27% of current workers and 41% of retirees were very confident about retirement. Meanwhile, the percentage of current workers and retirees who are "not at all confident"— 25% and 17%, respectively—essentially hasn't budged since the downturn.

Almost all of the increases in confidence occurred among households with incomes above $75,000. For households with lower incomes, daily expenses don't seem to leave much room for savings. Coincidentally, 53% of respondents in the survey cited a high cost of living to explain why they can't or won't save more.

Here are some other note worthy findings:

- Having a plan helps. Upper-income respondents were much more likely to participate in a 401(k) or other employer-sponsored retirement plan. The mere presence of such a plan seems to boost confidence in retirement saving.
- Many expect to work part-time in retirement. Almost two-thirds of current workers think they'll work during retirement to make ends meet. But only 27% of retires say they've been employed after retiring. The idea of working part-time in retirement is a common misconception.
- Count on a calculator. For respondents with an employer plan, EBRI used the Department of Labor (DOL) Lifetime Income Calculator to estimate monthly income in retirement. The DOL argues that this motivates workers to increase savings.

What about you? If you're not confident in your ability to save for retirement, we can help you create a realistic plan. ●

$2 Million For Retirement

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spend per year and still have an 85% chance of achieving their retirement goals? Running through a few scenarios provided an answer of $81,000. That's the amount they can spend each year and still have an 85% chance of never running out of money.

This raises another question: Is there a way for this hypothetical couple to spend $81,000 annually in retirement while also raising their probability of never running out of money? There are really just two ways to accomplish that, assuming that going back to work isn't a desirable option for them:

1. They could choose investments that deliver higher returns without increased volatility; or

2. They could look for investments that have the same returns, but less volatility.

One potential way to reduce volatility while maintaining reasonable levels of return is to acquire high-quality, dividend-paying stocks that have a history of increasing their dividends. If the volatility level is reduced from 16% to 13% per year, based on historical rates, the probability that this couple never will run out of money jumps from 85% to 93%. This significant leap is due to the fact that they are investing more heavily in stable, solid, dividend-paying stocks rather than in investment vehicles exposed to greater volatility.

Of course, everyone operates under a different set of circumstances. You might need to change several things from this base-bones example to meet your retirement goals. But it is difficult, if not impossible, to tell whether you will be able to retire comfortably until you sit down and actually run through the numbers. When that occurs, some interesting scenarios may emerge to help you see what you need to do to meet your goals.

Bottom line: Will $2 million be enough to sustain you through your retirement years? We can help you plug in the figures to give you a better grasp of your personal situation and then tailor your plan to your specific needs.●

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