Introduction to Retirement Planning

What is retirement planning?

Retirement planning involves an analysis of the various choices you can make today to help provide for your financial future. To make appropriate choices, you need to predict--as well as you can--your future economic circumstances. You'll also need to establish your post-retirement goals. When you've determined how much of an income stream you'll probably require in the future, you'll be in a position to make wise choices now about income, saving, investments, and employer-sponsored or other retirement plans.

Of course, you need to tailor your retirement planning to your own unique circumstances--planning methods may be different for employees and executives than for business owners. And no matter who you are, you'll probably want to gain some familiarity with the Social Security system, with post-retirement health care insurance coverage, including Medicare and long-term care (LTC) insurance. For some people, retirement may be an eagerly anticipated event, an opportunity to enjoy so many things that working may have precluded--travel, hobbies, and more family time. For other people, even the word "retirement" may conjure up feelings of fear or dread, particularly for those employees who work without the benefit of pension or other retirement plans. And newspaper stories predicting the collapse of the Social Security system can certainly compound anxiety. Whether you are financially comfortable or are of limited means, however, retirement planning is possible and can help you take control of your own future.

How can you determine your retirement income needs?

To determine your retirement income needs, you'll want to evaluate your present circumstances--your income, your expenses, your assets, and your debts. Next, you'll need to think about your future circumstances. There are four main sources for your retirement income: Social Security, pensions or other retirement vehicles, your investment portfolio, and savings. If you predict that your current income will not provide you with your desired retirement lifestyle, there are certain steps you can take now to help change your circumstances.

You'll want to think about your future sources of income, but also about where you'll live. Will you continue to live in your current home, for instance, or will you move to a condominium or retirement community? And if your employer typically provides early retirement packages to its employees, you'll need to know how to evaluate such packages from a number of perspectives.

How do you save for retirement?

Learning how to save for retirement is imperative. There are a number of retirement vehicles available, including traditional and Roth IRAs, employer-sponsored retirement plans, nonqualified deferred compensation plans, stock plans, and commercial annuities. Proper retirement planning requires an understanding of the workings of these tools.

In addition, your personal investment planning can help you on the road toward your retirement goals. The sooner you start, the longer you'll have to accumulate funds for retirement.

You'll want to understand the taxation of your retirement and investment vehicles. This is especially important since the enactment of the Jobs and Growth Tax Relief Reconciliation Act of 2003 (2003 Tax Act). The 2003 Tax Act reduced the capital gains tax rates and the tax rates of certain dividends, making the decision to allocate assets inside or outside a retirement plan more crucial.

Finally, you may want to learn strategies for handling the competing demands of educating your children and retiring.

What should you know about distributions from IRAs and other retirement plans?

Effective retirement planning involves not only an awareness of the types of savings vehicles available, but also an understanding of taking distributions from these vehicles. In particular, you should be familiar with the income tax ramifications of distributions (including a possible 10 percent premature distribution penalty tax for distributions made prior to age 59 ½). You may be interested in knowing whether you can borrow money from your retirement plan, whether it is better to receive your retirement money in one lump sum or in monthly checks, and whether you can roll your retirement plan balance into an IRA.

In addition, you may be concerned about naming one or more beneficiaries for your IRA or employer-sponsored retirement plan. What are the tax implications? What about required minimum distributions from the plan after you reach age 70½?