Buena Vista Investment Management, LLC

Creative Investment Solutions

RETIREMENT INVESTING October 2011

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1982 marked a beginning of a new era in retirement investing. Congress passed a bill that allowed people to invest $2000 each year into a retirement account and receive a deduction on their tax return. In the years that followed there have been numerous new retirement programs that have been added such as nondeductible IRAs, Roth IRAs, Simple-SEPs, and 401k accounts. The days of the defined pension plans have disappeared at most corporations. Thus the burden of saving and investing for retirement has been placed squarely on the individual's shoulders.

This transition of responsibility from corporations onto individuals means that investment decisions and strategies must be made by the stakeholder. With Finance not being a mandatory academic requirement in high school, there are many people who are not in a position to make informed decisions. Many custodians offer insights but really do not know all of the financial details of the people they are advising. It is my hope that people enjoy the same benefits of the old defined benefit programs, but my concern is that they will not.

There are many strategies that people employ in managing their investments. Here are some ideas that you might incorporate into your retirement planning:

1. Your age determines how aggressive or how conservative you want to be in your retirement accounts. The rule is that the closer you are to retiring the smaller your percentage of money should be in the equity markets. For people in their 20s and 30s, the vast majority of your dollars should be in stocks.

2. It is a solid tax strategy to have your mutual funds in your retirement accounts and if you buy individual stocks, they should be in your cash account. Mutual funds often distribute capital gains in the fall of each year. You never know how big or small these distributions might be. Thus it is not unusual to sometimes have tax payment surprises that are not pleasant. Individual stocks carry more risk than diversified mutual funds. It is not uncommon for an investor to have stocks that have not performed. In your cash account you can sell the loss and use it to offset gains against stocks you sold that had gains. Also you can write off up to $3000 each year from losses that exceed your gains against your income. You can also carry all of your losses forward to other tax years. Loses in your retirement account can't be used for tax purposes.

3. Bonds/CDs/Fixed income may also be most advantageous when bought in your retirement account. If you are in a 30% or higher tax bracket, you will lose in taxes $1 for every $3 of interest you earn. While in a retirement account you will be able to reinvest that $1. This compounding will have a significant effect if you have ten years or more before you need to use this money for budget purposes. Tax free bonds in most situations should not be used in retirement accounts.

4. Retirement accounts are tax deferred until you access the money. Annuities also are tax deferred. It makes no sense on a tax analysis to put annuities into accounts which are already tax deferred. In general, be careful when considering indexed annuities. These products often come with high surrender fees, high management expenses and limited investment options. Many indexed annuities come with guarantees but there are tradeoffs.

5. Only under extreme financial distress should you take money out of your retirement account before 59 ½. There is a 10% penalty for early withdraw and you have to pay both state and federal taxes. In a 30% plus tax bracket you could pay between 45-56% in taxes and penalties. This means for every $1 you take out you will be able to keep $.44-.55.

If you are frustrated by your current 401k due to limited choices and/or limited assistance may have some options that will relief some of that frustration. If you are 59 ½ or older most plans allow you to transfer out to an IRA rollover everything but the employer's contribution. This alternative allows you to have someone you trust manage the funds and a greater variety of investments that might better suit your investment needs.