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Projecting a Happy Retirement

Q&As on Roth 401(k)s

Finding and Claiming Forgotten Funds

I have matured U.S. savings bonds. Are they still earning interest and, if not, can I roll them over to another savings bond?



Callahan Financial Newsletter

Keeping you current

Projecting a Happy Retirement



A 2015 study found that 41% of households headed by someone aged 55 to 64 had no retirement savings, and only about a third of them had a traditional pension. Among households in this age group

with savings, the median amount was just \$104,000.¹

Your own savings may be more substantial, but in general Americans struggle to meet their savings goals. Even a healthy savings account may not provide as much income as you would like over a long retirement.

Despite the challenges, about 56% of current retirees say they are very satisfied with retirement, and 34% say they are moderately satisfied. Only 9% are dissatisfied.²

Develop a realistic picture

How can you transition into a happy retirement even if your savings fall short of your goals? The answer may lie in developing a realistic picture of what your retirement will look like, based on your expected resources and expenses. As a starting point, create a simple retirement planning worksheet. You might add details once you get the basics down on paper.

Estimate income and expenses

You can estimate your monthly Social Security benefit at ssa.gov. The longer you wait to claim your benefits, from age 62 up to age 70, the higher your monthly benefit will be. If you expect a pension, estimate that monthly amount as well. Add other sources of income, such as a part-time job, if that is in your plans. Be realistic. Part-time work often pays low wages.

It's more difficult to estimate the amount of income you can expect from your savings; this may depend on unpredictable market returns and the length of time you need your savings to last. One simple rule of thumb is to withdraw 4% of your savings each year. At that rate, the

\$104,000 median savings described earlier would generate \$4,160 per year or \$347 per month (assuming no market gains or losses). Keep in mind that some experts believe a 4% withdrawal rate may be too high to maintain funds over a long retirement. You might use 3% or 3.5% in your calculations.

Now estimate your monthly expenses. If you've paid off your mortgage and other debt, you may be in a stronger position. Don't forget to factor in a reserve for medical expenses. One study suggests that a 65-year-old couple who retired in 2015 would need \$259,000 over their lifetimes to cover Medicare premiums and out-of-pocket health-care expenses, assuming they had only median drug expenses.³

Take strategic steps

Your projected income and expenses should provide a rough picture of your financial situation in retirement. If retirement is approaching soon, try living for six months or more on your anticipated income to determine whether it is realistic. If it's not, or your anticipated expenses exceed your income even without a trial run, you may have to reduce expenses or work longer, or both.

Even if the numbers look good, it would be wise to keep building your savings. You might take advantage of catch-up contributions to IRAs and 401(k) plans, which are available to those who reach age 50 or older by the end of the calendar year. In 2016, the IRA catch-up amount is \$1,000, for a total contribution limit of \$6,500. The 401(k) catch-up amount is \$6,000, for a total employee contribution limit of \$24,000.

Preparing for retirement is not easy, but if you enter your new life phase with eyes wide open, you're more likely to enjoy a long and happy retirement.

¹ U.S. Government Accountability Office, "Retirement Security," May 2015

² *The Wall Street Journal*, "Why Retirees Are Happier Than You May Think," December 1, 2015

³ Employee Benefit Research Institute, Notes, October 2015

Q&As on Roth 401(k)s



Which is the better option, pretax or Roth contributions?

The answer depends upon your personal situation. If you think you'll be in a similar or higher tax bracket when you retire, Roth 401(k) contributions may be more appealing, since you'll effectively lock in today's lower tax rates. However, if you think you'll be in a lower tax bracket when you retire, pretax 401(k) contributions may be more appropriate. Your investment horizon and projected investment results are also important factors.

The Roth 401(k) is 10 years old! With 62% of employers now offering this option, it's more likely than not that you can make Roth contributions to your 401(k) plan.¹ Are you taking advantage of this opportunity?

What is a Roth 401(k) plan?

A Roth 401(k) plan is simply a traditional 401(k) plan that permits contributions to a designated Roth account within the plan. Roth 401(k) contributions are made on an after-tax basis, just like Roth IRA contributions. This means there's no up-front tax benefit, but if certain conditions are met both your contributions and any accumulated investment earnings on those contributions are free of federal income tax when distributed from the plan.

Who can contribute?

Anyone! If you're eligible to participate in a 401(k) plan with a Roth option, you can make Roth 401(k) contributions. Although you cannot contribute to a Roth IRA if you earn more than a specific dollar amount, there are no such income limits for a Roth 401(k).

Are distributions really tax free?

Because your contributions are made on an after-tax basis, they're always free of federal income tax when distributed from the plan. But any investment earnings on your Roth contributions are tax free only if you meet the requirements for a "qualified distribution."

In general, a distribution is qualified if:

- It's made after the end of a five-year holding period, *and*
- The payment is made after you turn 59½, become disabled, or die

The five-year holding period starts with the year you make your first Roth contribution to your employer's 401(k) plan. For example, if you make your first Roth contribution to the plan in December 2016, then the first year of your five-year holding period is 2016, and your waiting period ends on December 31, 2020. Special rules apply if you transfer your Roth dollars over to a new employer's 401(k) plan.

If your distribution isn't qualified (for example, you make a hardship withdrawal from your Roth account before age 59½), the portion of your distribution that represents investment earnings will be taxable and subject to a 10% early distribution penalty, unless an exception applies. (State tax rules may be different.)

How much can I contribute?

There's an overall cap on your combined pretax and Roth 401(k) contributions. In 2016, you can contribute up to \$18,000 (\$24,000 if you are

age 50 or older) to a 401(k) plan. You can split your contribution between Roth and pretax contributions any way you wish. For example, you can make \$10,000 of Roth contributions and \$8,000 of pretax contributions. It's totally up to you.

Can I still contribute to a Roth IRA?

Yes. Your participation in a Roth 401(k) plan has no impact on your ability to contribute to a Roth IRA. You can contribute to both if you wish (assuming you meet the Roth IRA income limits).

What about employer contributions?

While employers don't have to contribute to 401(k) plans, many will match all or part of your contributions. Your employer can match your Roth contributions, your pretax contributions, or both. But your employer's contributions are always made on a pretax basis, even if they match your Roth contributions. In other words, your employer's contributions, and any investment earnings on those contributions, will be taxed when you receive a distribution of those dollars from the plan.

Can I convert my existing traditional 401(k) balance to my Roth account?

Yes! If your plan permits, you can convert any portion of your 401(k) plan account (your pretax contributions, vested employer contributions, and investment earnings) to your Roth account. The amount you convert is subject to federal income tax in the year of the conversion (except for any after-tax contributions you've made), but qualified distributions from your Roth account will be entirely income tax free. The 10% early-distribution penalty generally doesn't apply to amounts you convert.²

What else do I need to know?

Like pretax 401(k) contributions, your Roth contributions can be distributed only after you terminate employment, reach age 59½, incur a hardship, become disabled, or die. Also, unlike Roth IRAs, you must generally begin taking distributions from a Roth 401(k) plan after you reach age 70½ (or, in some cases, after you retire). But this isn't as significant as it might seem, because you can generally roll over your Roth 401(k) money to a Roth IRA if you don't need or want the lifetime distributions.

¹ Plan Sponsor Council of America, *58th Annual Survey of Profit Sharing and 401(k) Plans* (2015) (Reflecting 2014 Plan Experience)

² The 10% penalty tax may be reclaimed by the IRS if you take a nonqualified distribution from your Roth account within five years of the conversion.



Do you have a tax refund waiting for you?

Each year, millions of dollars in tax refunds go unclaimed. In March 2016, the IRS announced that it was holding \$950 million in unclaimed refunds as a result of taxpayers failing to file a federal income tax return for 2012. (Source: IR-2016-38, March 10, 2016)

You may have missed out on a potential tax refund because you earned income and had taxes withheld but weren't required to file a tax return, or if you were eligible for refundable tax credits (where the amount of the credit you qualify for exceeds the amount of tax you owe). Even if you did file a tax return, your refund may have been undeliverable if your address was incorrect.

For more information on finding and claiming missing federal income tax refunds, visit irs.gov.

Finding and Claiming Forgotten Funds

As a child, you may have dreamed about finding buried treasure, but you probably realized at an early age that it was unlikely you would discover a chest full of pirate booty. However, the possibility that you have unclaimed funds or other assets waiting for you is not a fantasy.

According to the National Association of Unclaimed Property Administrators (NAUPA), \$41.7 billion is waiting to be returned by state unclaimed property programs. So how do you find what is owed to you, even if it's not a fortune?

State unclaimed property programs

Every state has an unclaimed property program that requires companies and financial institutions to turn account assets over to the state if they have lost contact with the rightful owner for one year or longer (such as when the account has been inactive). It then becomes the state's responsibility to locate the owner. State-held property generally can be claimed in perpetuity by original owners and heirs.

For state programs, unclaimed property might include the following:

- Financial accounts
- Stocks
- Uncashed dividend or payroll checks
- Utility deposits
- Insurance payments and policies
- Trust distributions
- Mineral royalty payments
- Contents of safe-deposit boxes

To see whether you have unclaimed assets, you may have to search your state's database and the databases of states where you formerly lived or worked. It's possible that funds or assets are still waiting for you even if you moved away years ago. Fortunately, most states participate in a national database that you can search for free at MissingMoney.com.

Finding "lost" life insurance policies might take some legwork. Life insurance companies that can't locate a beneficiary must generally turn over benefits from an individual policy to state unclaimed property programs, but might not do so if the company does not know that the policy owner has passed away. If you believe that a family member owned life insurance but can't find the physical policy, you may need to look for evidence of it by searching personal records and files (assuming you have the authority to do so) or by contacting the policy owner's insurance agent, attorney, or other financial professionals.

Federal unclaimed property programs

The federal government also tracks unclaimed property, including:

- Tax refunds
- Pension funds
- Funds from failed banks and credit unions
- Funds owed investors from U.S. SEC enforcement cases
- Refunds from FHA-insured mortgages
- Unredeemed savings bonds that are no longer earning interest

Unlike states, the federal government does not have a central website for finding unclaimed money or assets, so you'll need to check a number of sources, including one of the biggest sources of unclaimed funds--the IRS--at irs.gov. To find out more about other federal programs that may hold unclaimed property, visit the NAUPA website, unclaimed.org.

Submitting a claim

To claim property, follow the instructions given, which will vary by the type of asset and where the property is held. You'll need to verify ownership, typically by providing information about yourself (such as your Social Security number and proof of address), and submit a claim form either online or by mail.

What if the listed property owner is deceased? A claim may be made by a survivor and will be payable according to state or federal law. For life insurance, you may need the full name and Social Security number of the deceased individual, a copy of the death certificate, and in some cases proof that you were the named beneficiary.

Be careful

Private companies may be paid to locate rightful owners and/or offer to help rightful owners obtain property for a fee, but legitimate companies will ask you to pay only after you receive your property. State laws limit fees companies charge, so check with your state before you sign any agreement. However, in most cases you should be able to find the same property for free by checking state or federal databases. Carefully check out anyone who contacts you, because some scammers will claim to have property or represent that they are from a government agency in order to obtain other information about you or your finances. For more information about protecting yourself, visit the Federal Trade Commission's consumer information site, consumer.ftc.gov.

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I have matured U.S. savings bonds. Are they still earning interest and, if not, can I roll them over to another savings bond?

Once U.S. savings bonds have reached maturity, they stop earning interest. Prior to 2004, you could convert your Series E or EE savings bonds for Series HH bonds. This would have allowed you to continue earning tax-deferred interest. However, after August 31, 2004, the government discontinued the exchange of any form of savings bonds for HH bonds, so that option is no longer available.

Since matured savings bonds no longer earn interest, there is no financial benefit to holding on to them. If you have paper bonds, you can cash them in at most financial institutions, such as banks or credit unions. However, it's a good idea to call a specific institution before going there to be sure it will redeem your bonds. As an alternative, you can mail them to the Treasury Retail Securities Site, PO Box 214, Minneapolis, MN 55480, where they will be redeemed. If you have electronic bonds, log on to treasurydirect.gov and follow the directions there. The proceeds from your redeemed bonds can be deposited directly into your checking or savings account for a relatively

quick turnover.

Another important reason to redeem your matured savings bonds may be because savings bond interest earnings, which can be deferred, are subject to federal income tax when the bond matures or is otherwise redeemed, whichever occurs first. So if you haven't previously reported savings bond interest earnings, you must do so when the bond matures, even if you don't redeem the bonds.

Using the money for higher education may keep you from paying federal income tax on your savings bond interest. The savings bond education tax exclusion permits qualified taxpayers to exclude from their gross income all or part of the interest paid upon the redemption of eligible Series EE and I bonds issued after 1989 when the bond owner pays qualified higher-education expenses at an eligible institution. However, there are very specific requirements that must be met in order to qualify, so consult with your tax professional.



How many types of government savings bonds are there, and what's the difference between them?

While the U.S. government has issued 13 types of savings bonds, there are currently only two series available for

purchase through the U.S. Treasury Department: Series EE bonds and Series I bonds. U.S. savings bonds are nonmarketable securities, which means you can't resell them unless you're authorized as an issuing or redeeming agent by the U.S. Treasury Department. Savings bonds are guaranteed by the federal government as to the timely payment of principal and interest.

You can buy Series EE bonds and I bonds in any amount from \$25 up to \$10,000, which is the maximum amount you can purchase for each bond type per calendar year. In other words, you may buy a total of \$10,000 annually in both EE and I bonds, for an annual total of \$20,000 for the two types combined.

Series EE bonds earn a fixed rate of interest as long as you hold them, up to 30 years. You'll know the interest rate the bond will earn when you buy it. The U.S. Treasury announces the rate each May 1 (for new EE bonds issued between May 1 and October 31) and November

1 (for new EE bonds issued between November 1 and April 30).

Series I bonds are similar to EE bonds, but I bonds offer some protection against inflation by paying interest based on a combination of a fixed rate and a rate tied to the semi-annual inflation rate. The fixed rate component doesn't change, whereas the rate tied to inflation is recalculated and can change every six months. The total interest (fixed and inflation adjusted) compounds semi-annually.

In any case, the interest on EE or I savings bonds isn't paid to you until you cash in the bonds. You can cash in EE bonds or I bonds any time after one year, but if you cash them out before five years, you lose the last three months of interest.

The interest earned on both EE and I bonds is generally exempt from state income tax but subject to federal income tax. Interest income may be excluded from federal income tax when bonds are used to finance higher-education expenses, although restrictions may apply.

