Your Income Sources *after Retirement*

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University of Idaho
College of Agriculture
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Almost everyone looks forward to retirement, but most people have little idea how they will meet their income expectations after that last paycheck. Your retirement income and lifestyle will be dependent upon one or all of the four primary sources of retirement income: Social Security benefits, an employer-sponsored retirement plan, personal savings, and income from working after retirement.

This publication outlines each source to help you plan your future income. Complete worksheet 1 to get an overview of your own expected income sources in retirement.

Social Security plan

Knowing the amount you will receive from Social Security will help you plan your total retirement package. Social Security provides a base level of income for most retired people. It is not intended to replace all lost earnings. When your retirement date approaches (about 3 months before you want benefits to start) be sure to apply for Social Security benefits at your nearest Social Security office. These benefits do not automatically begin when you leave your job.

Eligibility for benefits

Eligibility for Social Security benefits requires meeting the earnings requirements yourself or being married to someone who does. A nonworking spouse at age 65 is eligible for half the benefits of the eligible spouse when the eligible spouse retires. If both you and your spouse work in covered occupations, your spouse will be eligible for a benefit based either upon his or her own earnings or upon 50 percent of yours, whichever is greater.

A spouse who collects Social Security at age 62 will get only 37.5 percent of the worker's benefits. A divorced spouse who had been married for at least 10 years can receive benefits at age 62 whether or not the former spouse receives them.

How retirement age affects benefits

Eligibility for full benefits comes at age 65 for people retiring now. However, you can retire any time after age 62 if you are willing to take a permanent benefit reduction. The reduction is 20 percent if benefits start at age 62; 13 1/3 percent if benefits start at age 63; and 6 2/3 percent if they start at age 64.

Because of longer life expectancies, the eligibility age for full retirement will be increased in gradual steps until it reaches age 67. This change starts in the year 2000, and it affects people born in 1938 and later. Reduced benefits will still be payable at 62, but the reduction will be greater than it is now.

Social Security offers you several incentives to remain on the payroll beyond the normal retirement age. First, your eventual benefit will be higher. Second, if you work until you are 70, you will receive full benefits regardless of how much you earn in retirement. And third, if you work beyond age 65, you will be entitled to a special bonus. The bonus, known as the delayed retirement credit, increases your benefits for each year you work between the ages of 65 and 70.

How years worked and earnings affect benefits

Besides depending on your age, the amount of your Social Security benefit depends on how long you have worked and on your average earnings. To get a Social Security retirement check, you must have received credit for a certain amount of earnings under Social Security. Generally, you must

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have worked 40 quarters or 10 years. (People who are 60 to 65 years old and are retiring now need 34 to 39 quarters.)

Not everyone who works that long will get a Social Security check. If you are paid by a nonprofit organization, most of your working years probably won't count toward earning a Social Security benefit. Only employment since January 1, 1984, at a nonprofit institution will be used in the benefit formula, unless Social Security taxes have been paid all along. About one-third of employees of state and local governments and all federal employees hired before January 1984 aren't covered by Social Security. Federal government workers hired since then are covered.

Keeping track of your benefits

Once you have met the Social Security requirements, you will never lose your eligibility, even if you never work again. Any credit you earned, regardless of changes in your employment status, is maintained under your Social Security number.

To be sure that your earnings record is correct, check your Social Security records every 3 years. Ask for form SSA 7004-SM-OPZ, "Request for Statement of Earnings," and mail the completed form to Social Security Administration, Salinas Data Operations Center, 100 E. Alvin Drive, Salinas, CA 93906-2494. Compare the year-to-year totals with your year-end W2 forms and report any discrepancy to the Social Security Administration.

Estimating your benefits

When you are within a few years of retirement, ask the local Social Security office for a copy of the free booklet SSA Publication no. 05-10070, *How Your Retirement Benefit Is Figured*. The formula for determining your Social Security benefit is complicated and subject to change. The Social Security Administration is the best source of information; however, you can roughly estimate benefits for planning purposes by following the steps on page 5.

Example: A 40-year-old person earns $35,000 a year or $2,917 a month before taxes. To estimate the effect of inflation on wages during the next 25 years before retirement at age 65, multiply the current monthly salary by 3.39 (table 1). The resulting preretirement monthly salary is $9,889.

Persons earning $35,000 now get about 25 percent of their wages replaced by Social Security retirement benefits (table 2). Twenty-five percent of $9,889 yields an estimated monthly benefit of $2,472.

Note: This example is for a single person. If both you and your spouse will use your own earned benefits, figure them separately and sum.

Employer-sponsored plans

The following information will help you understand the crucial elements of your company's employee pension plan. Essentially, there are two types of plans, the *defined benefit plan* and the *defined contribution plan*.

Defined benefit plan

A defined benefit plan is a pension plan under which the retirement benefit or amount you are to receive in the future is determined by the plan's benefit formula. A defined benefit plan requires that the employer contribute enough into the pension fund over the years to ensure that your retirement allowance equals the amount prescribed by the formula.

How to estimate your Social Security benefits

Step 1:

Multiply your present gross monthly salary by a factor equal to expected inflation (table 1):

$ ________	x	________	=	$ ________.
Present monthly gross salary		Inflation factor		Monthly salary you can expect to earn just before you retire

Table 1. Inflation factor at 5 percent inflation rate level.

Years until you retire	Inflation factor
1	1.05
2	1.10
3	1.16
4	1.22
5	1.28
6	1.34
7	1.41
8	1.48
9	1.55
10	1.63
15	2.08
20	2.65
25	3.39
30	4.32

Note: The table assumes an inflation rate of 5 percent—the average rate over the past 25 years.

Step 2:

Use table 2 to estimate the percentage of your wages that Social Security will replace. Table 2 assumes regular employment until you retire and average earnings increases.

Table 2. Percentage of wages Social Security replaces.

Your present yearly earnings ($)	Probable percentage of earnings replaced (%)
10,000	48
15,000	41
20,000	36
25,000	33
30,000	28
35,000	25
40,000	23
45,000	20
50,000	18

Step 3:

Multiply the monthly salary you expect to earn just before retirement (step 1) by the percentage of earnings you expect Social Security to replace (table 2). The result is an estimate of your monthly Social Security retirement check:

$ ________	x	________	=	$ ________.
Monthly salary you expect to earn just before you retire		Probable percentage of earnings replaced		Estimate of your monthly Social Security retirement check

An example of a possible benefit formula might be:

Percentage benefit factor x Years of service x Average salary = Annual retirement benefit.

Consider the case of a retiree who has worked 25 years at $35,000 per year and whose employer's benefit factor is 2 percent. He would compute his annual retirement benefit as follows:

.02 x 25 years x $35,000 = $17,500.

Your retirement allowance will be highest when it is based upon the earnings in your last year or in the final few years of service when you are likely to be earning the most. Least favorable is a plan that figures your pension as the average earnings for all years.

If you retire at age 65, annual benefits from traditional defined benefit plans are limited by the 1986 Tax Reform Act to $90,000 or 100 percent of your average compensation for your high 3 years, whichever is less. The ceiling lowers to $72,000 for people who retire at age 62. The tax law allows collection of no more than $38,000 a year for anyone retiring at age 55. (This is the pension you might get upon retiring from a $150,000 a year job).

Some employers fund the program entirely. Others require or permit employees to contribute. The company assumes all the investment risk in either case. It must make up the difference if the return on the investment falls short of the amount promised you.

The Pension Benefit Guaranty Corporation, a federal agency that insures defined benefit pensions, will protect yours to some extent if the fund is terminated and the plan is taken over by the agency. The maximum guaranty of benefits is $1,900 a month.

The pension insurance program covers most plans with set benefits, but not all "defined benefit" plans are insured. For example, if you work for doctors, lawyers, dentists, architects, or other professionals who employ 25 or fewer people, your plan is not insured. Government pension plans, plans run by religious institutions, union dues plans, and certain plans for company executives are not covered by the pension insurance program.

To cut costs many employers are shifting away from defined benefit plans, which guarantee you a certain predetermined income, to defined contribution plans.

Defined contribution plan

In this plan the employer contributes a fixed amount each year to a retirement fund that invests the money in a variety of ways. Under the rules of some plans, each year's contribution is set in advance. For example, the plan might call for 3 percent of each participant's salary or one-third of the year's net after-tax income to be contributed to the fund. Under other defined contribution plans, the employer decides each year what amount to contribute to the retirement plan.

Your retirement benefit is determined by the account balance when you retire. The amount of your account balance equals accumulated contributions plus earnings the fund produced, so the amount you eventually collect depends on how much you and your employer put in and how well the funds were invested. Defined contribution plans *are not* insured by the Pension Benefit Guaranty Corporation.

Some defined contribution plans require or allow contributions by employees. The employee's costs in a contributory plan are usually between 3 and 10 percent of wages and are generally paid through payroll deduction.

Examples of some defined contribution plans are salary reduction plans (401(k) plans); 403(b) plans; after-tax savings

plans; profit-sharing plans; employee stock ownership plans (ESOPs); stock purchase plans; and simplified employer pension plans (SEPs).

Salary reduction plans or 401(k) plans—This is an employer-sponsored plan that postpones taxes on both the investment earnings and on your contributions until you begin withdrawing them at retirement. An advantage of this plan is that your employer may contribute from 25 cents to a dollar for every dollar you put into the plan, up to 5 or 6 percent of your pretax pay. In addition, you won't owe Social Security taxes (FICA) on the money contributed by your employer.

Many employers fully vest employees in 401(k) plans after only 2 years and let you transfer the money to a new 401(k) if you change employers. (Refer to Time Required for Vesting, page 9, for a definition of vesting.)

The contributions go into one or more of several investments selected by the plan trustees. You decide how to divide the money among the investments, making you, in effect, your own pension manager. You hold the investment risk, but you also are the beneficiary of any gains.

Typically your investment choices will range from company stock or a diversified stock fund to a government securities fund or guaranteed fixed interest contract with an insurance company. Periodically you may choose to change your selections.

Federal tax laws limit the amount you can contribute to a 401(k) plan. For example, the maximum amount you can contribute in 1994 is $9,240 or 25 percent of your pay, whichever is less.

The tax code curtails your ability to withdraw money from an account before you turn 59½ years old. If you take out savings before then you generally have to pay a 10 percent penalty to the Internal Revenue Service in addition to regular income taxes on the withdrawal.

403(b) plans—These plans are similar to 401(k)s, but they are offered to employees of nonprofit organizations. Employee contributions, along with those of the employer, accumulate tax free until withdrawn at retirement. The funds may be administered directly by the employer or invested in mutual funds or annuities that you select.

After-tax savings plans—After-tax savings plans offer investment choices similar to those of 401(k) plans. Usually the employee is permitted to contribute between 2 and 6 percent of after-tax pay to the program. The company matches your contribution by as much as 100 percent, but usually 25 to 50 percent.

Some companies require you to work a specified period—usually 3 to 5 years—before you become eligible for the maximum matching contribution. Contributions are placed in a trust fund and invested by trustees who keep track of all employees' shares.

Profit-sharing plans—Under a profit-sharing plan the employer contributes money to an investment fund for each employee, and the money becomes the property of the employee when vested. A company may also allow you to contribute up to 5 to 10 percent of wages or salary. Taxes on earnings are deferred, and profits are held in trust. The investing usually is done by banks and professional investment counselors under the supervision of the plan's trustees.

A profit-sharing plan does not promise a specific benefit at retirement. This is usually because the employer's contributions may be linked to company profits, which can fluctuate. The investment skills of the plan manager can vary as well.

Employee stock ownership plans (ESOPs)—Employee stock ownership plans (ESOPs) are also classified as pension plans. The primary difference between ESOPs and most pension plans is that the assets of the plans generally consist of employer stock. These plans encourage employee participation in corporate ownership. The value of your benefit in an ESOP is directly related to the value of your employer's stock.

Stock purchase plans—Some large companies offer employees an opportunity to purchase shares of the company's stock under attractive terms. Usually you can designate as much as 3 percent to 10 percent of your after-tax salary each year to make purchases, buying shares at discounts and without brokerage fees. Your contribution is automatically deducted from each regular paycheck and placed in a special account that usually pays market rates of interest. At year's end, all the money in the account is used to purchase shares of company stock.

Simplified employer pension plans (SEPs)—Simplified employer pension plans make it possible for small-business owners to easily set up pension plans for themselves and their employees. Sole proprietors and self-employed workers such as freelancers and consultants can also set up SEPs.

A SEP is an IRA (page 10), but with much higher contribution limits. You are allowed to make your own contributions, as well as to decide where, among several investments, to invest the money.

There is no requirement that an employer contribute to your SEP-IRA. If the employer makes contributions, the contributions must be based on a written allocation formula and cannot discriminate in favor of officers, stockholders, and highly compensated employees.

The amounts employers contribute to a SEP vary depending upon profitability and other factors. The maximum permitted by law is also subject to change. Currently, the maximum amount that can be contributed to a SEP is 15 percent of compensation or $30,000, whichever is less. Contributions are tax deductible. The money is allowed to grow and compound tax free until withdrawn.

You take your SEP holdings with you if you quit, usually rolling the money over into a new employer's SEP or into an IRA. If you withdraw the money instead, you must declare it as income on the tax return and pay a 10 percent penalty. If you withdraw the money before turning $59^{1}/_{2}$, you must pay a 10 percent penalty.

Know your employer's plan

You may find it helpful to review a summary of your own company's plan rules. If you do not have a summary, often called a "summary plan description" or SPD, you should ask for one from the person in charge of your plan. Your company's personnel office or your union should be able to tell you who this person is.

Eligibility requirements for group pension plans

Most pension plans require employees to meet certain eligibility requirements before they can participate in the plan. Generally speaking, if your job is covered by a plan, you become a plan member within 6 months after you turn age 21 and after you have worked 1,000 hours in a year—20 hours a week for a full year or 40 hours a week for 6 months.

Time required for vesting

The term "vesting" refers to the absolute right of an employee to the benefits in a retirement plan based upon the employee's own contributions and the employer's contributions. Employees' contributions are vested immediately and can be withdrawn when the employee leaves the job. The rights of employees to employer contributions are generally subject to limitations, including service time requirements and amount limits.

Rules about when employees may enroll in the plan and about how years of service are counted toward vesting vary. Federal law specifies minimum requirements for qualified plans. For example, employees are allowed to participate in qualified retirement plans (defined benefit and defined contribution plans) beginning at age 21. Employers must count years of service since age 18 when counting time worked for vesting purposes.

There are three basic methods to determine vesting:

1. **Full and immediate vesting**. Your benefits are 100 percent vested once you meet the plan's minimum age requirements.
2. **Cliff vesting**. Your benefits are 100 percent vested once you complete 5 years of service. In multi-employer plans where more than one company pays into the plan, full vesting must come after no more than 10 years of service. Under a union contract, you have no vested rights until you complete this service.
3. **Graded vesting**. Your benefits are vested a little bit more each year. Graded vesting plans must vest workers 20 percent after 3 years of service, 40 percent after 4 years, 60 percent after 5 years, 80 percent after 6 years, and 100 percent after 7 years of service.

Note: These vesting provisions became applicable for plan-years beginning January 1, 1989. Before 1976, plans could require you to work a lifetime for one company before you earned any benefits. From 1976 until 1989, the usual requirement was 10 years of work.

Credit for years of service

How you earn benefits is usually determined by the number of years you work for your employer. You must know exactly how your employer counts a year of service.

Under most plans, you will have a year of service if you work at least 1,000 hours in a 12-consecutive-month period. Some plans give you credit for work performed before you became a participant, while others do not. Some plans use other standards for measuring years of service.

Any breaks in your service could affect the benefits you have accumulated. Check to be sure you have earned the pension benefits you think you have and that a break in service has not jeopardized your benefits.

To avoid losing some or all of your accumulated benefits because of a break in service, read your employer's booklet explaining the pension plan's provisions, particularly for break-in-service rules.

In general, you lose participation and vesting credits if your break in service (1) is for 5 or more years or (2) exceeds the number of years you were employed with the company before the break in service, whichever is greater.

Individual savings plans

The combination of Social Security and pension benefits is unlikely to give you the income you need. You can generally expect

the combination to replace no more than 40 to 60 percent of your salary. The rest will have to come from capital you build.

Remember to allow for inflation. For example, at a modest inflation rate of 3 percent you could expect a fixed monthly pension benefit to lose one-third of its purchasing power in only 11 years. Following are some supplementary savings plan options:

Individual retirement accounts (IRAs)

Individual retirement accounts (IRAs) are tax-deferred savings plans that allow individuals to contribute up to $2,000 annually ($2,250 with a nonworking spouse) into a government-approved retirement account. The interest you earn is tax deferred until you withdraw the money.

There may be other tax advantages as well. If you are not enrolled in a pension plan you may deduct the total amount of your IRA contribution from your income tax. If you are enrolled in other plans, all or part of your IRA contribution may be deductible, depending on your level of income.

For example, couples with an adjusted gross income of less than $40,000 ($25,000 for singles) can deduct IRA contributions in full. Couples with incomes of $40,000 to $50,000 ($25,000 to $35,000 for singles) can deduct a portion of their contribution. No deductions are allowed above these incomes. You can still make nondeductible contributions, however, and earn tax-deferred interest.

IRA's can be set up at a financial institution, brokerage company, mutual fund company, or insurance company. You can put many types of investments into this account, including certificates of deposit, money market deposit accounts, mutual funds, bonds, and stocks.

If you make a withdrawal from your IRA before you are age 59½, the distribution is subject to an early withdrawal penalty of 10 percent, unless you become disabled or die. Early withdrawals are also taxable as income.

Withdrawals must begin by April 1 the year after you reach age 70½. The rate of withdrawal must be such that it exhausts the IRA.

New tax laws regarding IRA rollovers—Employees who for any reason take lump-sum pension disbursements directly before retirement will receive only 80 percent of their money. The other 20 percent will be withheld automatically for taxes. You have 60 days to deposit the money in an IRA and thereby qualify to recoup the 20 percent when you file your income taxes, provided you deposit the full 100 percent.

You can sidestep these complications by asking your employer to transfer the money straight into an IRA. An IRA account may be rolled over only once in any 12-month period.

Keogh plans

Keogh plans are tax-deferred savings plans for self-employed workers. The amount of your contribution is based on your earnings.

For example, with a defined contribution plan your annual contribution may not exceed $30,000 or 20 percent of your income, whichever is smaller. A defined benefit plan, on the other hand, allows you to put the lesser of $118,800 or 100 percent of your compensation into a Keogh plan. Should you exceed these annual limits, you will be charged a 10 percent excise tax on the excess contribution.

Your investment choices are similar to those you would have under an IRA. You have the freedom to move from one investment to

another without tax consequences under a Keogh plan.

You can withdraw money from your plan at age 59½. As with the IRA, early withdrawals come with a 10 percent tax penalty, and you must begin withdrawals by age 70½. If you start a Keogh plan for yourself you must also set up one for each employee.

Annuities

Annuities are a type of savings plan designed to provide you with a steady income during your retirement years. When you purchase an annuity, you pay a predetermined amount to a company, which invests it. Then, at a specified age you get your money back, with interest, in a lump sum or in monthly installments for a specified number of years. Annuities are available through banks, savings and loan associations, brokerage firms, and insurance companies and come with a variety of options.

Certificates of deposit (CDs)

Certificates of deposit (CDs) are time deposits that mature at specific times, typically 6 months, 1 year, 2 years, and 5 years. Certificates of deposit may be purchased in denominations of $500, $1,000, $5,000, and above at a fixed rate of return. As a general rule, the longer the maturity and the larger the denomination, the higher the return.

Certificates of deposit are available from banks, savings and loan institutions, credit unions, and brokerage firms. Most CDs are federally insured for up to $100,000. (Check before you make a purchase.) There are penalties for early withdrawals, and the interest you earn is taxable.

U.S. government securities—Treasury bills, treasury notes, treasury bonds, and EE savings bonds

Treasury bills are short-term investments (either 3- or 6-month maturities). The minimum denomination is $10,000, with $5,000 increments thereafter.

Treasury notes have a fixed maturity of from 2 to 10 years and bear interest payable semiannually at fixed rates. They are available in minimum amounts of $1,000 for longer maturities and $5,000 for shorter maturities.

Treasury bonds have a fixed maturity of more than 10 years and are the longer counterpart of treasury notes. Yields on treasury bonds, because they are of longer maturity, are sometimes higher than on treasury notes.

Treasury bills, notes, or bonds may be sold prior to maturity at the current market rate, which can result in a yield greater or less than the original acquisition rate.

EE savings bonds are issued on a discount basis, which means you pay less than their full value, and their value gradually increases to full value. The difference between what you paid for the bond and what you receive at maturity or redemption is your interest.

The guaranteed minimum interest rate is 4 percent, compounded semi-annually up to its original maturity of 18 years. The market-based rate applies to EE bonds held 5 years or longer if the rate averages more than 4 percent.

All these government securities are guaranteed by the federal government. The interest is usually exempt from state and local income taxes. They are available without a sales fee at a federal reserve bank or for a small fee at other financial institutions and brokerage firms.

Money market deposit accounts (MMDAs)

Money market deposit accounts are savings accounts but pay the market rate of interest. MMDAs are insured and available through banks, savings and loan institutions, and some credit unions. You can have immediate access to your savings, but interest rates are usually very low.

Bonds

Bonds are issued through the government, federal agencies, municipalities, and corporations. Bonds usually provide a fixed, steady income and, in some cases, certain tax advantages. Bond prices can vary depending upon current interest rates. Some bonds are insured, while others are not. Bonds are available through brokerage firms and in mutual funds.

Mutual funds

Mutual funds pool money from thousands of shareholders and invest it with specific objectives. Mutual funds provide diversification of your assets, reinvestment of dividends, and professional management. A mutual fund's price per share fluctuates with the market, which means you could lose part of your principal.

How well the fund has performed in the past is no guarantee of its future performance. Mutual funds are not insured. They are available through brokerage firms for a fee or directly from mutual fund companies for lower fees or no fees.

Money market mutual funds

Money market mutual funds are a type of mutual fund that invests in CDs, government securities, and commercial paper (business and corporation loans and notes). The principal does not fluctuate; however, interest rates go up and down with the market. Although this type of investment is not insured, it is considered to be a low-risk investment. Money market mutual funds are available at brokerage firms, banks, and directly through mutual fund companies.

Stocks

Stocks may be traded through stock exchanges such as the New York Stock Exchange or over-the-counter. Stock prices are affected by fluctuations in the economy, political changes, corporate mergers, and the like. Information pertaining to various stocks is readily available from stockbrokers, newspapers, business magazines, and the companies themselves. Stocks are available through brokerage firms and some banks. Stocks are not insured.

Real estate investment trusts (REITs)

Real estate investment trusts allow shareholders to own real estate without the expense of sole ownership or the hassles of being a landlord. Real estate investment trusts are traded on the stock market. You can also invest in them through a mutual fund. Prices fluctuate with the real estate market and the stock market. This investment vehicle offers few tax advantages.

How much to save for retirement?

If you plan to be financially secure in retirement, you can expect to provide 40 to 60 percent of your annual retirement income with the capital you build. You should estimate how much capital it will take to make up that 40 to 60 percent income gap between your needed income and what you can expect from Social Security and your

employer-sponsored retirement plan. Refer to CIS 1013, *Your Financial Action Plan for Retirement*, to determine how much money you will need to meet your retirement goals.

Use table 3 to determine the monthly savings you would need to attain a predetermined amount of capital at age 65.

For example, if your goal is $500,000 and you begin investing when you are 25, you can reach it by saving $255 per month, assuming a 6 percent yield. If you wait until you are 45, you will need to save $1,065 per month, assuming a 6 percent yield.

Table 4 illustrates an individual making an annual IRA contribution of $2,000 for 9 years—from ages 22 through 30—and then making no further contributions. The illustration assumes the investment earns 8 percent annually. The result at age 65 will be a sizable retirement fund. On the other hand, if the individual begins annual contributions of $2,000 at age 31 and continues making them through age 65, he or she will have considerably less in the fund.

How long your savings will last

One way to visualize how long your savings will last is to use table 5.

Suppose at 65 years of age you have $500,000 growing at the rate of 8 percent a year and you begin withdrawing at an annual rate of 10 percent—$50,000 a year or $4,166.67 per month. The table indicates the savings will last 20 years or until you are age 85.

Retiring early

The decision to retire early voluntarily or through a company incentive program is a difficult one. Before quitting your job or accepting an incentive offer be certain to learn about your expected Social Security and pension benefits (additional or enhanced pension benefits for an incentive offer), retiree health insurance, and lump sum cash benefits. The inflation factor must also be built into the financial calculations you prepare.

Incentive programs are usually one-time offers. Employees must take advantage of them within a given time frame, usually referred to as a "window." Although you may have as long as 2 or 3 months to make your decision, in some cases the window may be open only for 1 to 2 weeks.

Quitting early means your savings must last longer than otherwise. Assuming a 4 percent average annual return after inflation, someone planning to retire at 55 has to put away $560,000 to collect $30,000 a year until age 90, compared with $468,000 for someone waiting until he or she is 65.

Table 3. Monthly savings needed at 6 percent interest (compounded annually) to attain a predetermined amount of capital at retirement.

Age now	Years to retirement	Desired amount at age 65			
		$200,000	$300,000	$500,000	$1,000,000
25	40	$102	$153	$255	$ 510
30	35	140	210	350	700
35	30	198	297	495	990
40	25	286	429	715	1,430
45	20	426	639	1,065	2,130
50	15	674	1,011	1,685	3,370
55	10	1,192	1,788	2,980	5,960

The younger retiree also has 10 fewer years to accumulate the cash reserve.

Many of the figures, tables, and examples presented are based on circumstances in 1994 and could change due to change in laws and/or economic conditions. **Always check current laws.**

Working after retirement

Working after retirement is often considered a fourth source of income for retirees.

Why should you work after you retire? To begin with, you may have no choice. Inflation, poor planning, or an inadequate pension may force the issue. Even if you don't need a job to make ends meet, you may decide you want one just to keep active and healthy.

Does it pay to keep working? If you're well off, you could wind up losing money by working. Social Security and tax code provisions penalize people who earn too much in retirement.

For example, if you go back to work in 1994 and you are between the ages of 62 and 64,

Table 4. The effect of saving early versus saving later. The example assumes savings in an individual retirement account (IRA) at 8 percent interest.

Age	Contributions made early	Contributions made later
22	$2,000	0
23	2,000	0
24	2,000	0
25	2,000	0
26	2,000	0
27	2,000	0
28	2,000	0
29	2,000	0
30	2,000	0
31	0	$2,000
32	0	2,000
33	0	2,000
34	0	2,000
35	0	2,000
36	0	2,000
37	0	2,000
38	0	2,000
39	0	2,000
40	0	2,000
41	0	2,000
42	0	2,000
43	0	2,000
44	0	2,000
45	0	2,000
46	0	2,000
47	0	2,000
48	0	2,000
49	0	2,000
50	0	2,000
51	0	2,000
52	0	2,000
53	0	2,000
54	0	2,000
55	0	2,000
56	0	2,000
57	0	2,000
58	0	2,000
59	0	2,000
60	0	2,000
61	0	2,000
62	0	2,000
63	0	2,000
64	0	2,000
65	0	2,000
Total investment	$18,000	$70,000
Amount available at age 65	$398,869	$362,412

you will lose $1 of Social Security benefits for every $2 you earn above $8,040. If you are 65 through 69, you will forfeit $1 in benefits for every $3 in earnings over $11,160. Once you reach age 70, you can earn as much as you like without penalty.

In addition, you will probably have to pay federal income tax on a portion of your Social Security benefits if the total of your adjusted gross income (AGI), tax-exempt income, and a percentage of your Social Security benefits exceed certain levels. On top of all this, your paycheck may push you into a higher tax bracket. Many states tax Social Security benefits, too.

Table 5. Number of years accumulated savings will last assuming specific interest rates and withdrawal rates.

Original principal withdrawn annually (%)	Interest earnings (%)										
	5	6	7	8	9	10	11	12	13	14	15
20	6	6	6	7	7	7	8	8	9	9	10
19	6	7	7	7	8	8	8	9	9	10	10
18	7	7	8	8	9	9	10	10	11	12	13
17	7	7	8	8	9	9	10	11	12	13	15
16	8	8	9	9	10	10	11	12	14	16	20
15	8	9	9	10	11	12	13	14	16	20	I*
14	9	10	10	11	12	13	15	17	22	I	
13	10	11	11	12	14	15	18	23	I		
12	11	12	13	14	16	19	24	I			
11	12	14	15	17	20	25	I				
10	14	15	17	20	27	I					
9	16	18	22	29	I						
8	20	23	30	I							
7	25	33	I								
6	37	I									
5	I										

Note: *I = Indefinite period of time.

For further reading—

CIS 1013	Your Financial Action Plan for Retirement	$1.00
CIS 973	Where to Live After Retirement	50¢
CIS 958	A Letter of Last Instruction: Everybody Needs One	75¢

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Worksheet – Estimating your retirement income

Sources of income	Monthly income	Annual income
Social Security plan		
* Worker at age ____	$ ______	$ ______
* Spouse at age ____	______	______
Employer-sponsored plans		
* Pension plan	______	______
* 401(k) or 403(b) plan	______	______
* Tax savings plan	______	______
* Profit-sharing plan	______	______
* Employee stock ownership plan	______	______
* Stock purchase plan	______	______
* SEP	______	______
* Other	______	______
Individual savings plans		
* IRA	______	______
* Keogh plan	______	______
* Income from annuities	______	______
* Interest income	______	______
* Savings accounts	______	______
* Certificates of deposit	______	______
* Money market deposit accounts	______	______
* U.S. government securities	______	______
Bonds	______	______
Mutual funds	______	______
* Dividend income		
Stocks	______	______
Insurance	______	______
Earnings from job	______	______
Rental income		
* Home (If any part is rented)	______	______
* Other real estate	______	______
Business owned by you	______	______
Gifts	______	______
Hobbies	______	______
Sale of nonincome-producing asssets (i.e., antiques, art work, automobile, jewelry)	______	______
Others	______	______
	Total monthly estimated income	**Total annual estimated income**
* Current dollars	$ ______	$ ______

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