

Retirement Plan Saving Considerations at Different Stages of Life *by Brent Yanagida, CFP®, EA*

Throughout your career, a retirement savings strategy will likely be one of the most important components of your overall financial plan. With most people planning for retirement expected to have annual expenses during retirement between 60% and 80% of their annual gross pay while working, it's obvious that Social Security alone will be far short of what one needs to live on when retired. This becomes even more acute when factoring in inflation on major retiree expenses such as medical costs. Recent studies (e.g., 2016 Retirement Health Care Costs Data Report by Healthview Services) show that an average 65 year-old retired couple today on Medicare and a supplemental policy living to age 87 (male) and 89 (female) should plan to have over \$300,000 in total medical costs (premiums and other out of pocket) in today's dollars. If we factor in historical medical cost inflation of between 5% and 6%, this couple should plan to have close to \$600,000 in inflated medical costs. For a 55 year-old couple, inflated costs could come close to \$1,000,000 for the same retirement period. These costs do not include possible costs for long term care.

The good news is that by having a savings plan throughout your life stages, you can not only cover your basic living and medical expenses in retirement, but also achieve your other retirement goals.

Retirement Saving Plan Stages

How should you view and manage your retirement savings plan through various life stages? The following are some points to consider depending on where you are at. We also know that everyone's situation will be unique and that retirement planning needs and strategies will also change over time.

Just Starting Out

If you are a young adult just starting your first job, chances are you face a number of differ-

ent challenges. Rent, college loans, and car payments all may be competing for your hard-earned yet still entry-level paycheck. How can you even consider setting aside money in your employer-sponsored or your own (IRA or Roth IRA) retirement plan now? After all, retirement is decades away — you have plenty of time, right?

Before you answer, consider this: The decades ahead of you can be your greatest advantage. Through the power of compounding, you can put time to work for you. Compounding happens when your plan contribution dollars and any company matches generate investment returns, and those returns continue to grow. Over time, the process can snowball.

Say at age 20, you begin investing \$4,000 each year for retirement. At age 65, you would have invested \$180,000. If you assume an arbitrary 5% average annual return on your investments, you would have accumulated a total of \$638,801 by age 65. However, if you wait until age 45 to begin investing that \$4,000 annually and earn the same 5% return, by age 65 you would have invested \$80,000 and accumulated a total of \$132,264. Even though you would have invested \$100,000 more by starting earlier, you would have accumulated \$506,536 more dollars overall.

That's the power you have as a young investor — the power of time and compounding. Even if you can't afford to contribute \$4,000 a year (\$333/month) to your plan, remember that even small amounts can add up through compounding. So enroll in a retirement savings plan and contribute whatever you can, and then try to increase your contribution amount by a percentage point or two every year. **A good target is to save at least 10% of your gross pay in early years for retirement, with the idea that you will increase to 15% or higher as you get into later stages of life. One should always take advantage of any com-**

As legislation becomes more certain on possible health care and tax law changes, we will incorporate such changes in our financial planning practices. We will also provide informational updates as needed and be available to discuss the impact that changes may have on your individual financial goals and strategies.

pany matches to a 401k type plan, regardless of how old you are.

There is also an opportunity, per current tax laws, for a taxpayer who is no longer a full time student to get a Retirement Savings Contribution tax credit (Saver's Credit) up to \$1,000 (\$2,000 if married) if one is contributing to an employer savings plan or IRA. This credit phases out if adjusted gross income is over \$31,000 (\$62,000 married). If you qualify, this can reduce your taxes dollar for dollar and shouldn't be passed up.

Finally, time offers an additional benefit to young adults — the potential to withstand larger short-term losses in order to pursue higher long-term gains. That means you may be able to invest more aggressively than your older colleagues, placing a larger portion of your portfolio in riskier investments such as a diversified stock portfolio to strive for higher long-term returns. If saving for a down payment on a house (or other large purchase) within a few years, one should save additional amounts outside a retirement plan, and you would likely want to use lower-risk investment options (e.g., savings accounts, CD's, shorter-term bonds) for these short term goals.

Getting Married and Starting a Family

You will likely face even more obligations when you marry and start a family. Mortgage or increasing rent payments, higher grocery and gas bills, child-care and youth sports expenses, family vacations, college savings contributions, home repairs and maintenance, and health-care costs all compete for your money. At this stage of life, the list of monthly expenses seems endless. **A key strategy should be to live within your means and not run up credit card debt that can't be paid off every month.** Living within your means also means owning the right-sized home if you are considering ownership over rental. If your estimated mortgage payments after a 20% down payment provide you with little room to save toward retirement, then perhaps you should reevaluate. Although it can be very tempting to cut your retirement savings plan contributions to make ends meet, do your best to resist temptation and stay diligent. Your retirement needs to be a high priority.

Are you thinking about taking time off to raise children? That is an important and often beneficial decision for many families. But it's a decision that can have a financial impact lasting long into the future. Leaving the workforce for prolonged periods not only hinders your ability to set aside money for retirement but also may affect the size of any pension or Social Security benefits you receive down the road. If you think you might take a break from work to raise a family, consider temporarily increasing your plan contributions before you leave and after you return to help make up for the lost time

and savings. Or perhaps your spouse could increase his or her contributions while you take time off.

Last, while you're still approximately 20 to 30 years away from retirement, you have decades to ride out market swings. That means you may still be able to invest relatively aggressively in your plan. But be sure you fully reassess your ability to withstand investment risk before making any decisions.

Reaching Your Peak Earning Years

The latter stage of your career can bring a wide variety of challenges and opportunities. Older children typically come with bigger expenses. College bills may be extensive. You may find yourself having to take time off unexpectedly to care for aging parents or other loved ones. Health-care expenses may be increasing. And those pesky home and car repairs never seem to go away.

On the other hand, with 20+ years of work experience behind you, you could be reaping the benefits of the highest salary you've ever earned.

With more income at your disposal, now may be an ideal time to kick your retirement savings plan into high gear. If you're age 50 or older, you may be able to take advantage of catch-up contributions, which allow you to contribute up to \$24,000 to your employer-sponsored plan in 2017, versus a maximum of \$18,000 for most everyone else. (Some plans impose different limits.). You should also consider saving into tax free accounts if qualified (i.e. Roth IRA's, Health Savings Accounts), and individual accounts. Regarding planning for upcoming college costs, contributing to a college savings plan (i.e. 529 plan) could be another strategy; however, keep in mind that one can easily borrow for college, whereas it is hard to borrow during retirement.

If you haven't already, you should have set goals regarding a retirement timeframe and lifestyle, list all your future sources of income, and with our help, run retirement projections to see if you are on track to reach your goals.

In addition, tax planning becomes more critical, and you should be working with your financial professionals to determine the best strategy to minimize taxes. Maximizing contributions into tax deferred savings plan can save substantial taxes in higher income years. If you are charitably minded, you might want to open up and contribute to a Donor Advised Fund to claim a larger tax deduction while in a high bracket, and yet have actual donations go to charities while in a lower tax bracket when any tax benefit would be limited or unavailable. NOTE: A future newsletter this year will likely provide more information about charitable contribution strategies as proposed tax law changes (if implemented) might make this year a good year to implement such strategies.

Preparing to Retire or Recently Retired

If you're considering retirement within the next five years or so, you're in the retirement "zone." This is a critical time period during which you'll be faced with a number of important choices, and the decisions you make can have long-lasting consequences. It's a period of transition: a shift from a mindset that's focused on accumulating assets for retirement to one that's focused on distributing wealth and drawing down resources. It can be confusing and chaotic, but it doesn't have to be. The key is to understand the underlying issues, and to recognize the long-term effects of the decisions you make today.

If you've recently retired, you're also in the retirement zone. You'll want to evaluate your financial situation in light of the decisions that you've already made, and consider adjusting your overall plan to reflect your current expectations and circumstances.

Your financial advisors can become a very important ally in helping to address the various decisions you will face at this important juncture. Besides reviewing any retirement plan projection created in the past, you may want to discuss:

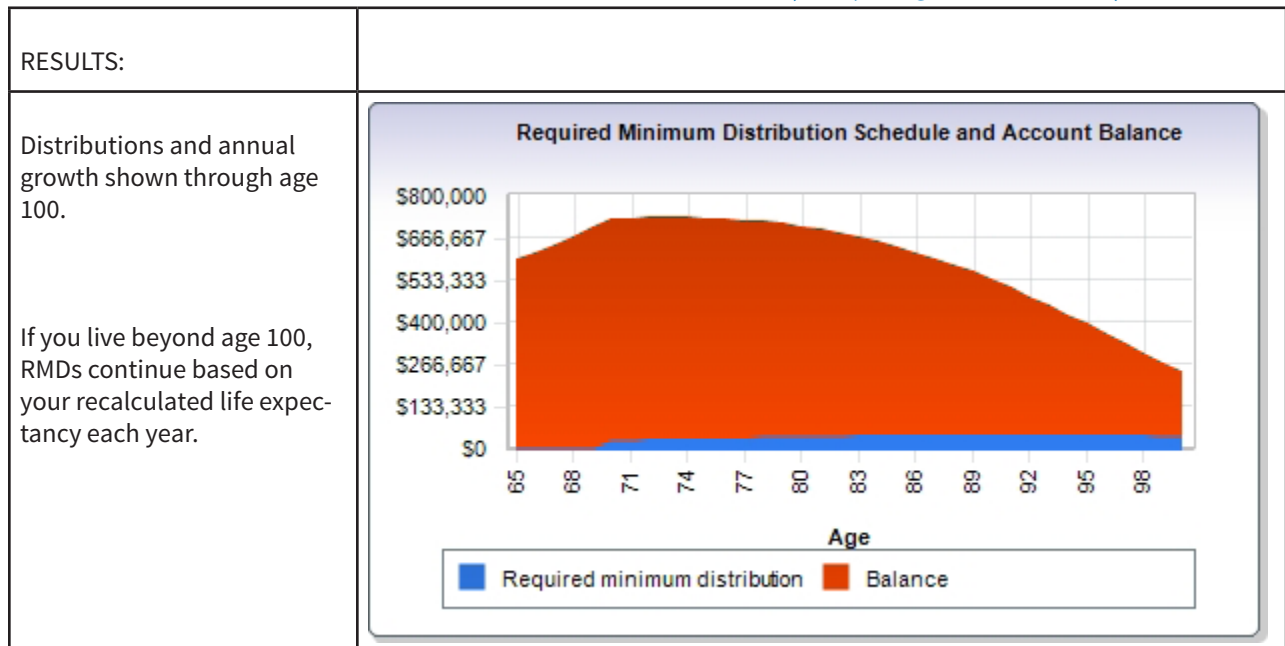
- Health care needs and costs, which may include health

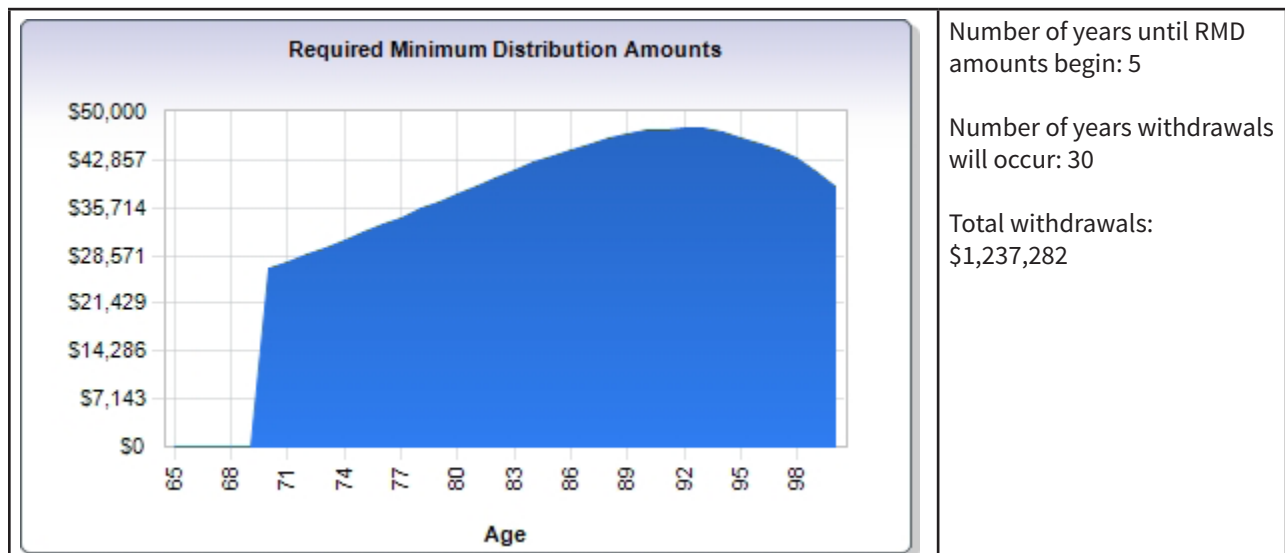
insurance prior to Medicare.

- Asset allocation changes, which typically include more cash and lower risk investments.
- A portfolio withdrawal strategy.
- Tax planning strategies.
- Social security claiming strategy.
- Reasons to tap into the equity of your home either through downsizing or through a government backed reverse mortgage.
- Part-time work or other sources of additional income.
- Estate planning (e.g., what and how much would you like to pass on to which beneficiaries).

You'll also want to familiarize yourself with required minimum distributions (RMDs) from your retirement saving plans. The IRS requires that you begin drawing down your retirement plan assets by April 1 of the year following the year you reach age 70½. If you continue to work for an employer past age 70½, you may be able to delay RMDs from that plan until the year following your actual retirement. The following graph shows an example of how a \$600,000 balance in an IRA or qualified plan at age 65 (assuming no more contributions) would change based on taking annual RMDs (second graph) while still making an arbitrary 4% annual return on your investments.

Traditional IRA Lifetime RMD Calculator Results (\$600,000 @ 4% annual ROI)





Number of years until RMD amounts begin: 5

Number of years withdrawals will occur: 30

Total withdrawals: \$1,237,282

Assumptions

Earnings are compounded annually.

You turn 70½ years of age in the calendar year in which you turn 70.

Your annual withdrawal equals the required minimum distribution amount each year. In any year, you can withdraw more than the required minimum. But if you withdraw less than the required minimum, you will be subject to a penalty under federal tax law.

Calculations are based on the Uniform Lifetime Table provided in the 2002 final IRS regulations. Special rules apply if your spouse is 10 or more years younger than you and is your sole designated beneficiary.

This is a hypothetical illustration only and not a projection or a guarantee of any particular investment performance.

Transitioning into Retirement: Are You Ready?

The first question that you should ask yourself is: “Am I ready to retire?” For many, the question isn’t as easy to answer as it might seem. That’s because it needs to be considered on two levels. The first, and probably the most obvious, is the financial side. Can you afford to retire? More specifically, can you afford the retirement you want? On another level, though, the question relates to the emotional issues surrounding retirement—how prepared are you for this new phase of your life? Consider both the financial and emotional aspects of retirement carefully; retiring before you’re ready can put a strain on the best-devised retirement plan.

There’s not always a “right” time to retire. There can be, though, a wrong time to retire. If you’re not emotionally ready to retire, it may not make sense to do so simply because you’ve reached age 62 (or 65, or 70). In fact, postponing retirement can pay dividends on the financial side of the equation. Similarly, if you’re emotionally ready to retire, but come up short financially, consider whether your plans for retirement are realistic. Evaluate how much of a difference postponing retirement could make, and then weigh your options.

Transitioning into Retirement: Non-financial Issues

When it comes to retirement, it’s easy to focus on the finan-

cial aspects of your decision to the exclusion of all other issues. But there are a number of non-financial issues and concerns that are just as important.

Fundamentally, your retirement income plan is just a means to an end: having the ability to do the things you want to do in retirement, for as long as you want to do them. But that presupposes that you know what it is you want to do in retirement. Many of us have never thought beyond the vague notion we’ve held during most of our working lives: that retirement—if properly planned for—will be something of an extended vacation, a reward for a lifetime of hard work. Retirement may be just that ... for the first few weeks or months. The fact is, though, that your job likely demanded your attention for a majority of your waking hours. No longer having that job leaves you with a lot of free time to fill. Just as you have a financial plan when it comes to your retirement, you should consider the type of lifestyle you want and expect from retirement as well.

What do you want to do in retirement? Do you intend to travel? Pursue a hobby? Volunteer your time? Take educational courses? Start a new business or part time career? Give some real thought to how you’re going to spend a typical week, and consider actually writing down a hypothetical schedule.

Having concrete plans can also help overcome problems commonly experienced by those who transition into retire-

ment without thinking ahead:

- Loss of identity--Many people identify themselves by their professions. Affirmation and self-worth may have come from the success that you've had in your career, and giving up that career can be disconcerting on a number of levels.
- Loss of structure--Your job provides a certain structure to your life. You may also have work relationships that are important to you. Without something to fill the void, you may find yourself needing to address unmet emotional needs.
- Fear of mortality--Rather than a "new beginning," some see the "beginning of the end." This can be exacerbated by the mental shift that accompanies the transition from accumulating assets to drawing down wealth.
- Marital discord--If you're married, consider whether your spouse is as ready as you are for you to retire. Does he or she share your ideas of how you want to spend your retirement? Many married couples find the first few years of retirement a period of rough transition. If you haven't discussed your plans with your spouse, you should do so; think through what the repercussions will be--both positive and negative--on your roles and relationship.

Working in Retirement

Many individuals choose to work in retirement for both financial and non-financial reasons. Per a recent study conducted by Bank of America Merrill Lynch and Age Wage, about half of retirees today either have worked or plan to work in retirement. The obvious advantage of working during retirement is that you'll be earning money and relying less on your retirement savings--leaving more to potentially grow for the future, and helping your savings last longer. But many retirees also work for personal fulfillment--to stay mentally and physically active, to enjoy the social benefits of working, or to try their hand at something new. If you are thinking of working during your retirement, you'll want to make sure that you understand how your continued employment will affect other aspects of your retirement, such as your taxes, or how your Social Security payments/strategy could change.

Caution: Many people who count on working full time until their mid-60s and working part time in retirement find that health problems or job loss prevents them from doing so. When making your retirement plans, it may be wise to consider a fallback plan in case everything doesn't go as you expect.

Considerations for All

Everyone should have an emergency cash fund while working and normally we would suggest 3-6 months of annual income as a cash safety net. Retiree cash funds will vary de-

pending on possible expenses and sources of income.

Throughout your working days, you may face other important decisions involving your retirement savings plan. For example, if your company savings plan provides for Roth contributions, you'll want to review the differences between these and traditional pretax contributions to determine the best strategy for your situation. This applies to traditional IRA's and Roth IRA's as well. While pretax or traditional IRA contributions offer an upfront tax benefit, you'll have to pay taxes on distributions when you receive them. On the other hand, Roth contributions do not provide an upfront tax benefit, but qualified withdrawals will be tax free, providing certain rules are followed. Whether you choose to contribute to a tax deferred account, a Roth account, or both will depend on a number of factors. In general, Roth type contributions are best if contributed to early and/or when in lower tax brackets.

If you have a year with lower taxable income due to a job change/layoff, or you retire before taking Social security and RMDs, tax strategies regarding your investment accounts should be considered. This could include IRA to Roth IRA conversions and/or capturing long term capital gains in a taxable brokerage account if the 0% federal tax rate (for those in 15% or lower marginal tax bracket) would apply.

In doing distribution and tax planning for retirees, having ample sums of money in the following three classifications of investment accounts provides for optimum planning opportunities.

1. Tax deferred money (i.e. 401k type plans, traditional IRA's)
2. Tax free money (i.e. Roth IRA's, Health Savings Accounts)
3. Taxable account money (i.e. individual/joint brokerage accounts), which can include tax efficient investments such as stocks, certain mutual funds/ETF's, and municipal bonds.

It's also important to consider what type of investment fits best in each account, and to know what investments are best to liquidate for cash. Your investment advisor should be a key resource in this area. While it's generally not advisable to make frequent changes in your retirement plan investment mix, you will want to review your plan's portfolio from time to time, especially as major events (e.g., marriage, divorce, birth of a child, job change) occur throughout your life.

Please know that we are here to help you plan and implement key financial strategies throughout your life stages. We encourage you to share this newsletter with others who might benefit. Our website, Peakam.com, will have this and past articles posted for easy reference, or we could send you additional copies if requested.

Company Profile: Gilead Sciences *by John McCorvie, CFA*

Gilead Sciences, Inc.'s stock (symbol: GILD) was added to our Model Portfolio* at the end of 2016. It had been on our watch list for many years. From our perspective, investors became overly optimistic on Gilead's stock in mid-2015 and then became overly pessimistic in 2016. Yes, Gilead's revenue dropped in 2016 (and is projected to decrease this year as well). Yes, there are real product challenges that Gilead is working through right now that could materially impact Gilead's future. However, when a stock price reaches a level where the big risks are already priced in, we get interested. In Gilead's case, we concluded that the potential reward in purchasing Gilead's stock far outweighed the potential risk.

Gilead is a successful biotech company that has built its core business on treatments for viral diseases, including drugs that suppress HIV/AIDS and cure Hepatitis C (yes, cure!). Gilead received its first FDA approval for treatment of HIV/AIDS in 2001 and is currently the leading provider of the drugs that have helped turn HIV into a manageable chronic condition (and also help prevent the spread of HIV). It received FDA approval for a Hepatitis C cure in 2013 and remains the leading provider. Gilead has improved the quality of life and extended the lifespan of millions of people in the U.S. and around the world. It continues to spend heavily on research and development to be able to offer additional treatments in areas ranging from liver diseases (including Non-Alcoholic Steatohepatitis (NASH) and Hepatitis B), to oncology, to inflammation diseases.

There are 3 key challenges that Gilead faces that will impact the success of the investment:

1. Gilead is currently transitioning HIV/AIDS treatment to its next generation drugs. To date the transition is going well and sales in HIV treatment grew 3% in the latest quarter. Completion of the transition, along with competition and patent expirations, are a threat to its core business.
2. Gilead's Hepatitis C sales have been falling since they peaked in 2015. After the initial surge when the cure became available, new prescriptions have been falling

(there is no recurring business from cured patients!). Throw in competition and lower pricing, and investors remain pessimistic about the sustainable level of future sales.

3. Gilead's research and development pipeline of new drugs has not had much success in the last couple of years and is not expected to materially contribute to sales until 2019. It is not surprising that many investors, in a "what have you done for me lately" mode, have become frustrated over not seeing an immediate and clear path to future growth. The pressure on Gilead to make a major acquisition to bolster future revenues is growing, but the success or failure that might come from such an acquisition is just one more unknown.

On the financial side, Gilead's revenue in the first quarter of 2017 came in at an annualized rate of \$26 billion, almost 17% below the previous year (Hepatitis C sales were down almost 40%), and its earnings came in at an annualized rate of about \$8 per share (and a little higher on a free cash flow basis), down almost 19% from the previous year. It currently pays a dividend of \$2.08 a share annualized, a 3% yield on the current stock price. On the balance sheet side, Gilead has more than enough cash and liquid investments to pay off all of its debt (and is accumulating more cash for potential acquisitions).

Gilead's stock is currently priced as if its business will be cut in half over the next few years and never grow again. While the stock market could be right, it is a pretty low bar. In one of the most expensive stock market environments in history, Gilead is a true "Value" stock. The potential of a business with the success, experience and resources of Gilead to outperform those low expectations is high.

The Model Portfolio is not a real cash portfolio. It represents the core direction of our portfolio management strategies. Individual client portfolios are managed in accordance with the clients' specific investment objectives and constraints. Historical results of specific securities are available upon request.

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