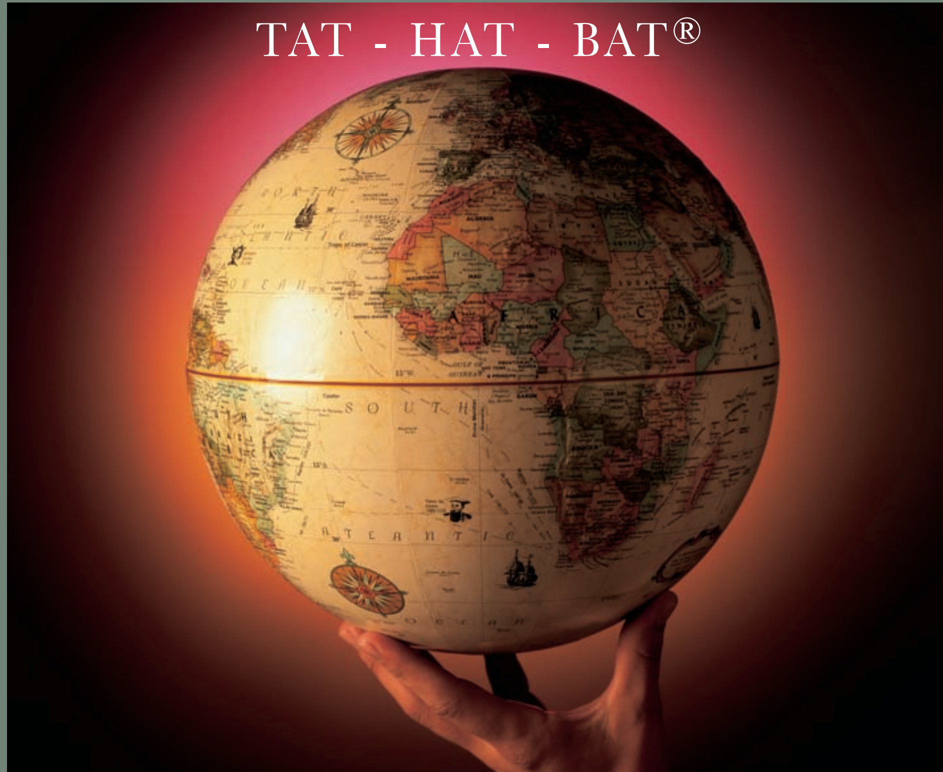
Show-Me Financial Freedom

A Guide to Missouri Public School Employees' Financial and Retirement Planning

Thank A Teacher -
Help A Teacher -
Be A Teacher®



www.lifelongteachers.net

By: Ron Finke and Mark Iglehart

Dedicated to Missouri public school employees and retirees.

"What the best and wisest parent wants for his own child--that must the community want for all its children. Any other ideal for our schools is narrow and unlovely; acted upon it destroys our democracy."

John Dewey

"When we do the best that we can, we never know what miracle is wrought in our life, or in the life of another."

Helen Keller

"I have come to believe that a great teacher is a great artist and that there are as few as there are any other great artists. Teaching might even be the greatest of arts since the medium is the human mind and spirit."

John Steinbeck

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Introduction

Why publish another financial guide when there are so many already? Not one existing document met our objectives of providing concise, useful information for Missouri public school employees. Although most of the information contained in Show-Me Financial Freedom is appropriate for anyone, it is tailored for you, the Missouri public school employee. It addresses a wide variety of financial and legal topics aimed at wise choices from early career through the rest of your life. However, it is not intended to provide specific investment or insurance purchasing advice for your individual situation.

We strived to condense the wisdom contained in stacks of financial resources into a booklet you can read in one or two sessions. However the Appendix contains a Bibliography of additional resources including publications and websites related to the topics covered. The more you know and understand about the basics of money, maximizing insurance choices, growing wealth and planning for enjoyable retirement years, the better outcome you and your family should enjoy. Above all, we hope you find it to be intensely practical. Making informed, wise decisions enables you to maximize the financial benefits possible from investing your life in helping Missouri students.

Many young people are called to the education field because they want to make a difference in others lives. Money is secondary. Fortunately, the current system can help you accumulate phenomenal investment assets over time, giving you the freedom to retire at an early age and enjoy the fruit of your savings for a very long period. But as with most of life's opportunities, you must supply the willpower to take advantage of them and overcome the roadblocks.

In an ideal world, school districts would devote in-service hours to help educate its employees on important benefit and retirement issues. Since this type of dedicated time is scarce in today's education climate, we believe that distributing this booklet and making it available on the internet at www.lifelongteachers.net are the most effective means of reaching the most districts and employees.

We feel strongly about this project because we have greatly benefited from our fantastic Missouri Public Education System. Furthermore, we believe strong public education is a major key to our country's success. Public education is the bridge to a child's dream without regard to one's socio-economic status.

You are the key to unlocking the potential of the next generation. We hope this information helps you enjoy a more rewarding career and gain personal financial freedom. In the process, you will also help keep Missouri public education strong and effective for decades to come.

Chapter 1 Start on Track: Learn the Basics

Consider five of the most successful professional athletes of recent US history: Lance Armstrong, Wayne Gretsky, Michael Jordan, Annika Sorenstam and Tiger Woods. Each one stayed at the pinnacle of his or her sport for at least seven consecutive years. But each started years earlier by learning and practicing the fundamentals of that sport. Having the spirit and desire of champions, they improved their skills and pushed themselves harder until they had the confidence to know they could compete and win in their chosen arena.

How does this relate to your personal financial success? To reach financial goals, you must learn the basic rules and practice the fundamentals. Unlike top athletes, you don't have to be gifted with unusual physical or mental attributes to win at this game, just a desire to learn and make wise choices. Thanks to our country's great systems of public education and free enterprise, you can have a decent income. So let's get started.

Financial Fundamental One:
Income Must Always Exceed Expenses Over Time.

The most critical truth of personal finance is that "it's not what you make, but what you keep that counts." The only way to become financially secure is to learn to spend less than you earn. It may not be easy to overcome past mistakes, bad habits or life events, but you can eliminate student loans, credit card, medical and other debts over time. Do not buy into the lie that any normal American life requires consumer debt. Those who fully understand the concept of interest make sure they receive it and those who do not, pay it.[1]

First, you must know what you spend in order to control it. Keep track on a calendar or simple ledger. Make it a daily habit[2]. Use the envelope method[3] to help you control impulsive spending, the greatest enemy of financial success. Inexpensive financial software programs are available for tracking your progress also.

In this first stage, the important questions are:

- What is my Cash Flow? (income, expenses and savings over a period)
- What is my Budget? (plan for income and spending)
- What is my Net Worth? (all current assets minus all debts)

[1] However, early in your career, one exception to this rule may be to invest in yourself through additional educational hours or specialized training that will help you to gain more responsibility and increase your future income stream.

[2] David Rockefeller recalls this fact about his father, John D. Rockefeller, one of the wealthiest men of our history. He was always willing to give his children money for their needs and reasonable wants but only if they could show him exactly how they had spent what he had already provided them. Accountability is lesson one of good stewardship.

[3] According to your spending plan, put cash into an envelope for each discretionary category such as eating out, entertainment or incidentals. When the cash is gone, there is no more spending in that category until next payday.

Financial Fundamental Two:
Take Murphy Out of the Competition.

Have you ever known anyone who has *not* had a financial emergency? Neither have we! The greatest planners still have unexpected illnesses, accidents, equipment breakdown or similar emergencies. Financial radio personality Dave Ramsey says we can blame poor Murphy and his Law for such circumstances. But you can eliminate most of Murphy's effects by having enough savings in an emergency fund. If you do not, Murphy seems to live with you as a combination best friend/worst nightmare.

First, be absolutely certain you are protected against those risks you cannot afford to take alone. This includes insurance to cover your automobile, disability, health, homeowner's or renter's (property and casualty), life and long term care. Buy all of the coverage you need for gaps in protection provided through your employer. Consider these insurance premiums to be the foundation of your savings plan.

Second, since insurance costs less when you share in the risk (deductibles, co-pays etc.), build up your emergency fund before you invest in any other longer term investment accounts. How much is enough? Begin with $1,000 as an absolute minimum but you should generally have at least four months worth of our routine expenses in very liquid form. The rate of return is not important—the ability to get the money within a week or two is paramount. There are many money market funds available today that pay reasonable interest and allow you to write checks. Keep this money separate so you can count on it. When you have to use some for a bona fide emergency, save up again until the fund is replenished.

Financial Fundamental Three:
Maximize Your Individual Employment Benefits.

Starting any new position brings excitement along with many new responsibilities and opportunities. You should learn about and properly enroll in your employer provided insurance and retirement plans. This is an important fundamental that will help you and your family to as it relates to your present and future security.

Employers go to great lengths and expense to offer competitive fringe benefits to attract and retain quality employees. It is not uncommon for an employer to spend $10,000 or more per year per employee on fringe benefits. Understanding and choosing wisely the plans paid for you as well as ones offered to you by payroll deduction is a vital first step toward your financial freedom. Remember that concerning financial matters, there is no such thing as a dumb question except perhaps why you did not ask for help. Use the provider company representatives working with your district. Service to you is why they exist. If there are none, seek out a financially savvy administrator or associate and ask them for help.

Financial Fundamental Four:
Take Advantage of Tax-Free Employment Benefits.

A tax-free dollar is the most valuable. It is actually a dollar earned and a dollar kept. Employer paid health insurance, term life insurance—up to $50,000, sick days, and a few other plans do not require that you pay any taxes on the premiums paid by the employer for you. Therefore, a $5,000-a-year payment by your employer for your health insurance policy is worth the entire $5,000 to you. To look at it another way, if you were required to pay the $5,000 from your earnings, you would need to earn $6,350 or more (depending on your tax-bracket). This is because you pay federal, state and possibly Social Security and Medicare taxes on earned income. *You are not taxed on your "qualified" employer provided benefits.*

For example, many people pay 25% federal and 6% Missouri income tax on their highest bracket of income. Therefore they would have to pay an additional 31% for an equivalent benefit they had to provide for themselves with taxable income. To determine the advantage of tax free benefits to you, calculate your marginal combined income tax rate (federal and state tax rate on the highest portion of your adjusted gross income--or ask your tax preparer for it) and divide the cost of the benefit by (1 minus r) where r = highest marginal income tax rate. Therefore:

$$\frac{\$1{,}000}{1-(.31)} \text{ equals } \frac{\$1{,}000}{.69} \text{ equals } \$1{,}449.28 \text{ (per \$1,000 of benefit)}$$

You don't have to teach math to see that $449.28 of tax is well worth saving! Not only are premiums not taxable income to you but the benefits you receive are also tax free.

Financial Fundamental Five:
Take Advantage of Tax-Deferred Savings and Investment

To the Internal Revenue Service, a dollar is a whole dollar only until you actually receive it as income. At that point, it is less! Your regular income may be $2,500 per month, but that is before taxes. However the contributions you and your employer pay into the Missouri retirement system are tax-deferred. Therefore, you do not pay federal and state income taxes on these contributions and earnings until you receive them back in the form of a monthly retirement benefit, a partial lump-sum or a complete lump-sum withdrawal. In the meantime investment managers work hard to safely grow the contributions tax-free. Withdrawals from the retirement system are not allowed until you terminate your employment from Missouri public schools. (This latter rule is the reason why school employees enjoy one of the very best levels of retirement income relative to career earnings of any industry.)

You can also save in other retirement plans on a voluntary basis with tax-deferred dollars. These plans are known by their tax code section numbers such as 403(b), 457, 401(k), and 408. English language terms for them include Tax Deferred or Tax Sheltered Annuities,

Deferred Compensation Plans and IRA's. Review the following example to determine how this type of savings works to your advantage and consult your personal tax adviser with respect to your specific tax situation.

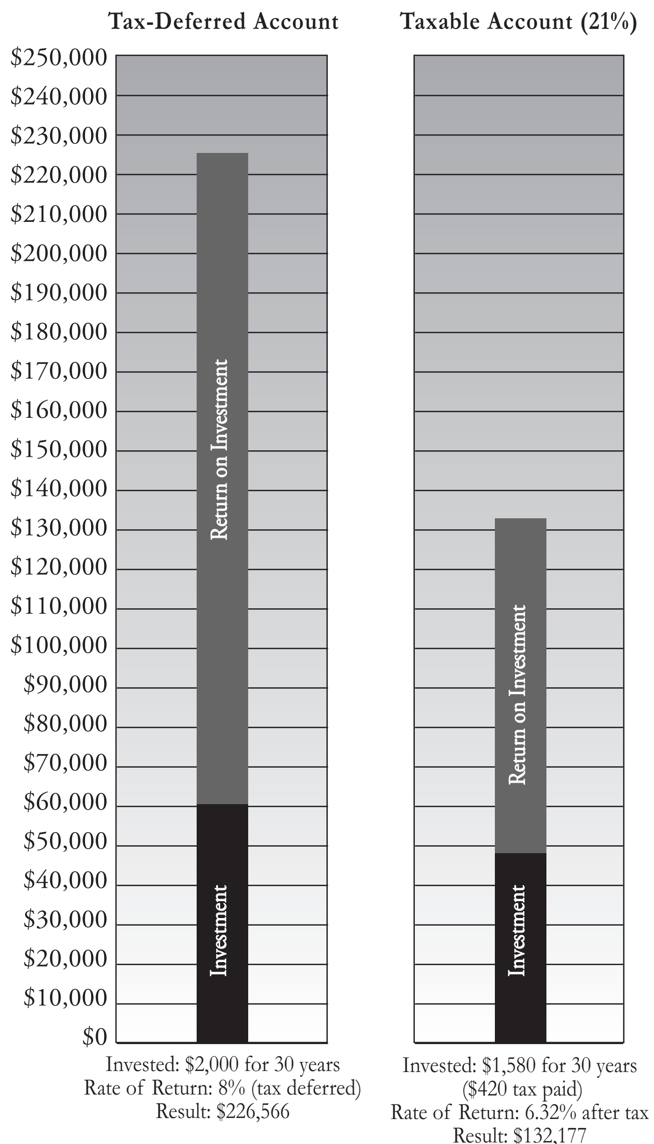
Example 1.

Assume that you save $2,000 per year for retirement in addition to your required pension contributions. A 403(b) plan allows you to invest the entire amount. If instead you invest in a taxable account, such as a Bank Certificate of Deposit, you can only invest $1,580 after tax.[1] Further assume you continue to save and invest that amount for thirty years and earn 8% compounded over that period. In the taxable account, also assume you must pay tax annually at long term capital gains rates. What is the resulting difference?

	Tax-Deferred Account	**Taxable (21%)**
Invested:	$2,000/year for 30 years	$1,580 for 30 years ($420 tax paid)
Rate of Return:	8% (tax deferred)	6.32% after tax
Result:	$226,566	$132,177

Taxable savings is also important but the initial tax deduction and tax deferral on investment earnings make a significant difference.

* 8% is used for illustrative purposes only and is not intended to represent current or expected investment returns.



[1] Many employees today pay 15% federal and 6% Missouri income taxes on their highest marginal income. You can find your marginal tax rate by using the tax tables or by consulting your income tax preparer. This is not an average tax rate but it is the rate one should use to determine the cost or benefit of tax deductibility and/or deferral.

Financial Fundamental Six:
Know the "Rule of 72" to Make Time and Compounding Work for You.

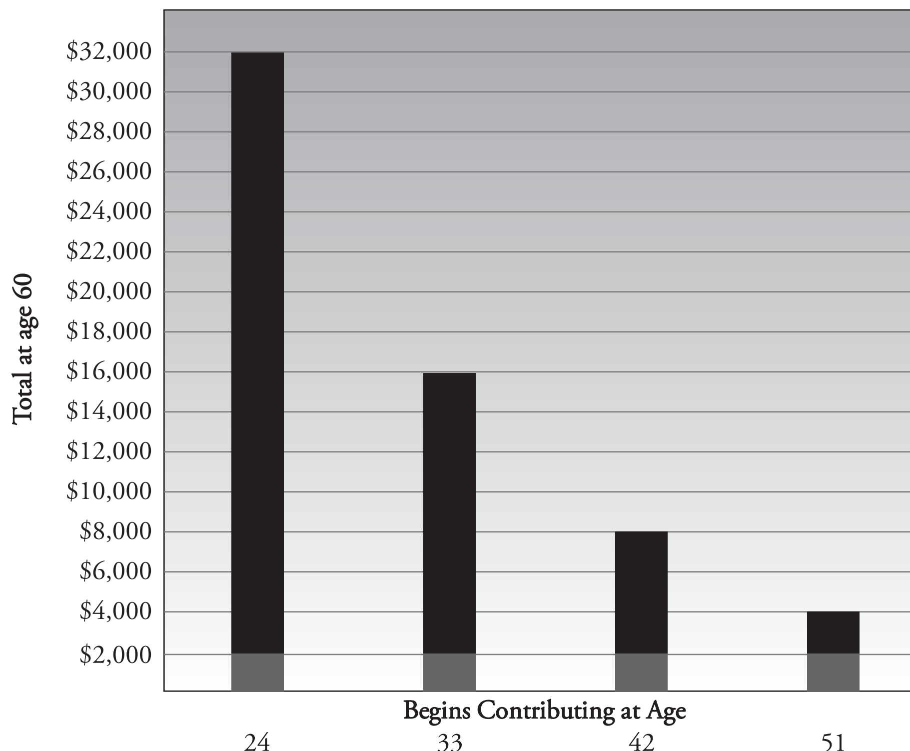
Albert Einstein, the mathematical and physics genius of the early 20th Century, called compound interest the "eighth wonder of the world." It bears repeating that when you truly understand it, you will want to collect it (by investing) and will not want to pay it (by borrowing). Learning the Rule of 72 is a simple way to appreciate the effect of time upon compounding of interest. The formula for finding the time period required for invested money to double in value is the annual interest rate of return you receive divided into the number 72. Mathematically it looks like this:

> T = 72/r where r = the annual rate of return and T is the number of years required for doubling to occur.

Therefore, if you could invest in a certificate of deposit at an after-tax rate of 8% for nine years, your initial investment will have doubled (72/8% = 9). At 6%, it would take twelve years (72/6% = 12) and so on. That fact may not seem life changing but consider what happens with greater lengths of time. The following example should make the point.

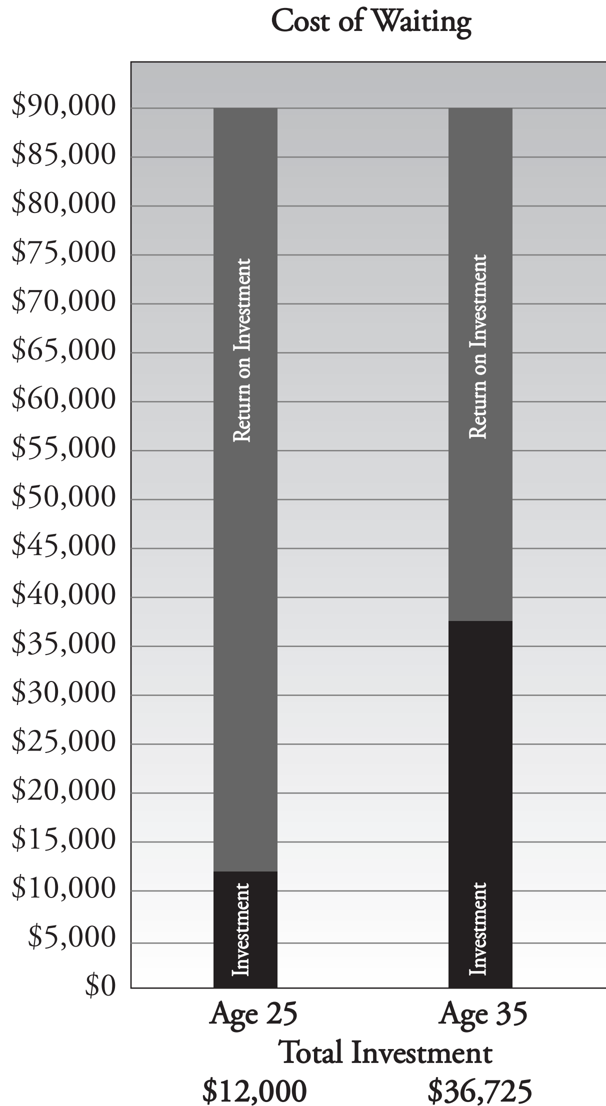
Example 2.

Suppose that you invest that first $2,000 at age 24 and your tax qualified account earns 8% for the next thirty-six years. At 33, the account has grown to $4,000; at 42, to $8,000; at 51, to $16,000 and at 60, to $32,000—all from a one-time $2,000 hidden away. What if you wait until 33 to begin? Then you have $16,000 at age 60, half as much. If you wait until 42, then you will have $8,000 or one fourth as much.



Example 3.

But what if you cannot afford to save $166.67 per month at age 24? Can't you just put in more money later? The answer is "Yes but you may first want to see the cost of waiting." Suppose you contributed just $100 each month for ten years and then quit but let the balance grow another twenty years until age 55. The resulting balance is just over $90,000. How much will it take per month if you wait to begin until age 35 and contribute for twenty years? Answer: $153. Let's review: Option 1, $12,000 invested earlier. Option 2, $36,725 invested later. The cost of waiting ten years to start is 200% more in total contributions.



The best means of using compounding to your advantage is to pay off any consumer debt as quickly as possible, save whatever amount you can each month in your early adult years and increase the dollars invested as your salary increases. If you invest $100 per month for the first ten years and then $153 per month for twenty years, you double the balance by age 55 and have over $180,000.

Chapter 2 Employer Provided Benefits

How Do I Take Maximum Advantage of My Group Health Insurance?

Begin your consideration of medical insurance with the truth in mind that there is no such thing as a free lunch. The cost of any group insurance plan consists of the amount required to pay the claims incurred by the employee group, an amount to pay for the administrative process and an amount for profit or reserve in order for the insurance company or self-insured group to continue operating. For decades the cost of medical care has inflated at rates two to three times that of most goods and services. Therefore we should not be surprised that the cost for a good group policy per employee may be more than $500 per month and over $1,200 for family coverage.

Because of this higher rate of inflation, employers in all industries have had to reduce benefit levels provided to employees or increase deductibles or amounts payable up front known as co-pays. Limiting or eliminating benefits when you seek treatment from certain medical providers are additional cost-containment mechanisms. These changes not only reduce employer costs but are designed to give you the consumer a strong incentive to use your health care benefits wisely, not as though they are free. Consumer Driven Health Plans (CDHP) also align with the widely known statistic that generally 20% of the population accounts for 80% or more of total health care expenditures.

The key to making these benefits work well for you personally is your own personal attention and education about the details. Whether you are just beginning your teaching career or in your twentieth year, take a small period of concentrated time to study the basic operating parts of the plan. You have plenty to do and you may prefer watching paint dry but the money you save will be your own!

Pay special attention to the deductible or co-pay amounts mentioned above, the percentage split between your cost and the amount paid by the insurance carrier (co-insurance), the incentives built in to encourage you to use certain providers (doctors, hospitals, therapists, etc.) and finally, the total risk you personally bear for expenses for yourself and your family (often called the out-of-pocket maximums). Your district may also sponsor a cafeteria plan that allows you to save pre-tax an amount deducted from your paychecks to pay toward your personal costs.

What Is a Cafeteria Plan?

Cafeteria Plan rules and guidelines are contained in the Internal Revenue Code Section 125. Different components of an employer sponsored Cafeteria Plan include:

- Cash (doesn’t change your tax situation)
- Insurance Premium Conversion
- Medical Expense Flexible Spending Plan
- Dependent Care Expense Account

Unless you choose cash, your Cafeteria Plan selections are tax-free, which helps increase your take-home pay as explained in Financial Fundamental Four.

With the **Premium Conversion Plan**, you pay your portion of the premium on certain qualified plans, including employer health insurance premiums, dental, vision, supplemental health, cancer, accident, and up to $50,000 of group term life insurance (less any employer paid term life benefits) with pre-tax dollars. The way it works is simple. You direct a portion of your salary to be deducted from your gross pay (before taxes) for the employer to use to purchase these benefits for you. Since the employer pays, neither the premiums nor benefits are taxable to you.

There are restrictions on the types of employer sponsored insurance plans that qualify, as well as when you can make changes to your election during the plan year. Check with your employer or your plan administrator for further information. Internal Revenue guidelines must be followed.

Since these plans and rules can seem complicated, sometimes well-meaning family members or friends may discourage you from participating. Remember, only you can make the best decision after you take initiative and become properly informed.[1]

With the **Medical Expense Flexible Spending Plan**, you can also set aside pre-tax dollars from your salary (again a salary redirection into your account) to cover certain tax qualified un-reimbursed healthcare expenses (including mileage to and from appointments) for you and your family members. During the plan year, when you incur eligible, un-reimbursed healthcare expenses (including over the counter medications and contact solutions) you simply use your Flex Plan Debit Card at the point of service, or complete and file a simple claim form with your receipts to your plan administrator. You'll be reimbursed by the plan administrator for these expenses, up to your annual plan contribution. Best of all, you are avoiding income taxes on these expenses, putting more money in your pocket or in your supplemental retirement savings program.

But plan wisely because if you or eligible family members haven't incurred eligible expenses to cover your annual election by the end of the plan year, the unused balance is forfeited. Therefore, be realistic and conservatively estimate your expenses, but remember you don't want to leave your hard-earned money on the Tax Man's table![2]

[1] Author Iglehart recently was visiting with his wife and two of her teacher associates when questions arose about their district's benefits re-enrollment. One said she did not participate in the Premium Conversion Plan although she paid almost $900 monthly for health and dental coverage for her husband and children. As he explained the difference of tax-free premiums, she realized by signing up for the Premium Conversion Plan she would save enough in taxes to contribute $200 a month to her child's 529 College Savings Plan.

[2] The Igleharts had two daughters both in orthodontic braces during a two year period. By redirecting $7,000 into the Cafeteria Plan during that time, they saved about $2,000 in Social Security, federal and state taxes. The second teacher in the conversation (see in note 1) mentioned she was paying $200 per month to an orthodontist for her daughter. Once she understood how easy it was to participate, she also enrolled in the Medical Expense Flexible Spending Plan and saved significant tax dollars.

If you have a child under age 13 for whom you pay for part-time or full-time day care, you may be able to save taxes by contributing to a **Dependent Care Expense Account** if your employer provides this option. Some restrictions apply concerning caregiver details and the same "use it or lose it" rules apply to amounts not spent from your account by the end of the allotted time. In this case, you must determine whether you will be better off to take the Dependent Care Tax Credit available to most parents on their personal income tax return rather than using the Dependent Care Expense Account.

With respect to any Cafeteria Plan tax-saving opportunities, a knowledgeable advisor can quickly help determine your best alternatives. Your employer benefits too when you participate in the Cafeteria Plan because it wants happy employees with more take-home pay. The employer saves money too because it does not have to pay Social Security or Medicare tax on dollars sheltered by the employees. So by understanding the principles of tax-free, tax-deferred and taxable money, you will be able to increase your take-home pay and your long term investing, thus improving your odds of achieving financial freedom.

What Benefits Do I Receive as a Substitute for Social Security?

As of July 1, 2008, each certificated school employee has 26% of his/her total compensation deposited into the Public School Retirement System (PSRS) and thereby receives a package of benefits in the event of death, permanent disability or retirement. You contribute half of this amount by payroll deduction while your employer contributes the other half. Since this mandatory contribution is a higher percentage than the tax rate for Social Security, the long term benefits are also higher. Like the federal program, PSRS provides a retirement income benefit (also known as a defined benefit pension) determined by a formula based upon years of credited service multiplied by the average of the employee's highest consecutive three years of monthly compensation. Employee Health Insurance premiums paid by the district are added to this figure, thus increasing one's future retirement benefit.

The Public Education Employees Retirement System (PEERS) covers employees who don't hold a current Missouri Teaching Certificate. The benefits operate in a similar manner but PEERS members also participate in Social Security. As of July 1, 2008 the employee and employer contribute 6.25% into the PEERS system to fund its benefits and 6.2% into Social Security. In addition to these benefits, both PEER and PSRS members pay 1.45% of pay as federal Medicare tax and his/her employer matches that amount.[1] Therefore, each retiree shall have full Medicare benefits at age 65 as long as he/she meets the Medicare service credit requirements whether by educational or other service.

In many cases a thirty year employee can retire with retirement benefits equal to his net disposable income just prior to retirement. The wonderful PSRS/PEERS internet website provides a wealth of useful information and allows you to easily perform estimated benefit calculations at www.psrs-peers.org. PSRS/PEERS employees are also an outstanding resource to members. If you have questions regarding your benefits, beneficiary designations, retirement options, or upcoming retirement, you should contact them at (800) 392-6848.

[1] PSRS employees employed in the same district prior to 1986 may not be covered by Medicare through that district. Check with your local Social Security office for details about your own situation

What Is Vesting and Why Is It So Important to Me?

The PSRS/PEERS system requires five complete years of credited service before an employee is fully vested. This is known as cliff vesting because the benefit available to one who does not have five years of credit is simply a refund of his/her contributions.[1] If an employee leaves before five years are completed and later withdraws his personal contributions, then he/she forfeits the employer's contributions to the retirement system. These forfeitures are used to fund death, disability and retirement benefits for those who are vested.

This factor becomes incredibly important with respect to an employee's permanent total disability benefit. If not fully vested, a disabled employee has no income insurance protection provided by the system. Therefore because disability is the greatest risk of financial ruin for younger employees up through middle age, each person needs to give serious consideration to purchasing a quality individual disability income policy unless his/her employer provides group disability insurance protection as an additional employer paid benefit. Be certain to have as much as 70% of your gross income protected.

After school employees become fully vested, the PSRS/PEERS system provides benefits similar to but better than those of the federal Social Security system. In addition to the disability income protection mentioned above, each vested employee has benefits for dependents in the event of pre-retirement death and of course an excellent retirement benefit with many alternative choices.

What If I Die Before Retirement?

Do you have someone who is depending upon you and your income for their support or standard of living? Apart from that, do you have someone you want to benefit in case of your death? If so, then you will be pleased to know that the PSRS/PEERS retirement system provides death benefits for those purposes.

This benefit is funded from both employee and employer contributions to the system. It is in addition to whatever group term life insurance your local district provides and what you may purchase through payroll deduction. Your beneficiary may choose one of three types of benefit depending upon their status and relationship to you.

A beneficiary may elect to receive a **Lump Sum** refund death benefit, a **Monthly Dependent-Based Survivor Benefit** or a **Monthly Retirement-Based Survivor Benefit**. The lump sum alternative may be the smallest amount in net present value but it is available for any beneficiary regardless of relationship with the employee. Only qualified dependents may choose among the others. In the case of Social Security benefits, there is no return of contributions unless dependent beneficiaries exist at the time of death.

[1] If the employee who terminates employment so chooses, he can leave his contribution balance in the system for up to five years and receive interest on the balance. If he returns to employment with a member employer within five years and receives at least one-tenth of a year of additional service, then he continues to accrue service credits as though he had not terminated. If he does not return within five years, the system will offer him a withdrawal of his balance and will not credit any further interest on it.

Chapter 3 Risk Management Products

Risk management is an important fact of life. There are an infinite number of risks we face but only a few critical enough to require insurance to help us deal with the consequences of the occurrence. For example you may by nature be at risk to lose your umbrella. You may have lost a dozen umbrellas during your life, but you do not need to insure against the risk of losing your current one? Start from the perspective that you should have insurance to protect yourself and your family from any risks so substantial that you cannot afford to face them alone. Following this principle will prevent you from being either over-insured or under-insured.

What Should I Know About Life Insurance?

Since physical death is a fact for everyone, its risk is only one of when and perhaps how. If we knew we would live to a point certain, we could also know how to plan and implement our life goals accordingly. Life insurance helps us to complete our goals and dreams if we are unable to finish them ourselves. When you cover this risk for a finite period of time, it is called term insurance.[1] A contract guaranteed to last for your physical life is permanent life insurance (also called whole life).

Changes in technology, life expectancy and financial products over the last quarter century or so have led to an explosion in the different forms and flavors of life insurance available to you. Because of competition and greater longevity, almost all life insurance premiums have actually declined in recent years. But at the heart of it, remember that each type is just a variation of term or permanent insurance.

Since term insurance resembles renting coverage for a lease term, look for guarantees of convertibility and renewability.[2] If you buy coverage for a term shorter than you are likely to need protection, try to be certain that you can afford higher future premiums when one term period ends and another begins. For a person in his/her twenties or thirties, a twenty or thirty year level term policy may be sufficient to protect through normal retirement age if all goes as planned.

On the other hand, permanent insurance is designed to have the term of protection equal to your actual lifetime. Some Companies will now specifically guarantee your benefit to age 120 or higher. The premium charged must at least fund the death benefit over your lifetime so a reserve, cash value, is created for you. You can buy variable policies that allow you to choose how, when and where you want cash value invested among sub-accounts resembling mutual funds. In other contracts, the insurance company invests conservatively in bonds, mortgages and real estate as allowed by law.

[1] Common forms of term insurance now include annual renewable as well as periods of 5,10, 20 and 30 years of coverage. Be careful to understand whether a contract has premiums that are guaranteed level for the entire term or has a schedule of premiums currently charged and a schedule of higher maximum premiums that the insurance company can charge if necessary to adjust for changes in their economic circumstances.

[2] Because of your high risk of being disabled, you should also buy the waiver of premium benefit so that the premiums will be paid for you after a few months if you should become disabled. This benefit will last until age 65 in the best contracts.

Mutual life insurance companies pay dividends on *participating* policies to you as a company owner. Tax law considers these a return of premium not taxable until you have withdrawn more total value than the accumulated premiums paid. Many policies allow variable premiums too so that you can invest extra money at times depending upon your cash flow.[1] In all permanent policies, the growth of cash value is otherwise **tax deferred** until you surrender your policy and it is **tax free** if paid out to your beneficiary at your death. Therefore permanent insurance receives favorable tax advantages because government finds it in the public interest to encourage savings and investing in this unique method that protects your loved ones in case of your disability and at your death.

One popular strategy today is called *Buy Term and Invest the Difference*. This presumes that you will buy a sufficient dollar amount of life insurance in the near term, but for only the time period necessary for you to save and invest enough money to meet your future objectives and become self-insured. It can be successful, *but only* if you are disciplined and successful in both saving enough money and investing it to hit your targets. Therefore you should only pursue this plan if you understand its limitations. Make certain you have enough income protection against the risk of disability that your standard of living and your required savings per month will continue in all events.[2]

How Much Life Insurance Do I Need?

"It depends" is not an answer we usually want. But life insurance is a unique financial product with special characteristics to help you manage your risk of dying before you are financially ready. What is your situation? Do you have a spouse only? How many children do you have now or plan to have? How much debt do you have to extinguish? Do you want to guarantee the money will be there for your children's education if they do their part in working hard to prepare, or rather allow them to get the money themselves as you did? Each of you has different answers that are right for you[1].

Rules-of-thumb include an amount ten to twelve times your annual income as a young adult to a more modest three times your income as your age, annual income and other financial assets increase. Many software programs also exist on the internet to help calculate the amount necessary to achieve your goals for those you leave behind. A quality financial advisor or insurance agent will also complete a diagnostic process in order to confirm that you are protecting your family as you desire.

If you use a reasoned approach to determining the right amount for you, then you can avoid being sold excessive death benefit or spending too much of your savings plan on only risk protection rather than also growing your investment net worth. However you can consider your life insurance

[1] In some circumstances, a policy can be funded so as to be in a *paid up* status in which the company guarantees the death benefit with no additional premiums. However, be aware that some agents incorrectly refer to the use of policy loans or dividend surrenders to pay policy premiums by this same terminology.

[2] Since you can only buy the best quality contracts at the best premiums while your health is good, consider initially buying at least a high quality term insurance contract with excellent conversion privileges as a guarantee toward your future needs and wants. Also most permanent insurance contracts offer a guaranteed insurability rider allowing you to buy additional amounts of protection at various ages such as every three years between 25 and 40 or upon occurrence of marriage or the birth of a child *even if you are uninsurable at the time.*

premiums as a form of savings. You should know that you have the correct amount of protection and the best kind of contracts to achieve your unique goals. Whenever you die, your family will not care whether you bought term or permanent life insurance. What will matter is whether you left them between a rock and a hard place or have provided them the resources they will need to financially succeed the rest of their lives.

How Much and What Kind of Disability Income Protection Should I Have?

Since everything else depends upon your monthly income, its continuation is critically important.[1] In the event of an accident or sickness that prevents you from fulfilling your duties, most education employers have a form of sick pay plan to help. Some provide employees with a number of full pay sick days per year with a maximum that can be accrued. Find out if you have an insured Short Term Disability plan that pays you a percentage of your salary for a few months after your sick days run out. You may also be covered with a Long Term Disability Group Insurance policy that pays a percentage of salary after a 3-6 month waiting period. Commonly the benefit is 60% or $66\frac{2}{3}$% and covered income does not include extra duty contracts.[2] PSRS also offers a disability retirement benefit option, but only if **your permanent** disability occurs after you are fully vested with five years service.

These policies vary widely so examine the fine print carefully. If you don't have enough group coverage, purchase your own individual policy. Your living expenses won't stop (and often increase) if you have to stop working. Try to obtain coverage referred to as guaranteed renewable with the definition of disability referenced to percentage income loss (often called residual), a guaranteed insurability rider, a cost of living adjustment rider and a benefit period to at least age 65.

How Much, What Kind and When Should I Buy Long Term Care Insurance?

Americans are living longer and often healthier lives. However if a severe disability leaves you unable to care for yourself, much less earn an income, who will pay for the additional care you need? Long-term care (LTC) includes a range of services for individuals that require assistance with activities of daily living such as:

- Bathing
- Dressing
- Eating
- Maintaining continence
- Toileting, and
- Transferring from a bed to a chair and back.

LTC also includes the supervision of someone with severe dementia or Alzheimer's disease.

[1] While 3% of home foreclosures are caused by death, 48% are caused by a disability. Housing and Home Finance Agency, U.S. Government, 1998. Of all 40 year old men disabled for at least 90 days, the average period of disability is 5.5 years. Social Security Administration estimates that a 20 year old worker has a 3 in 10 chance of being disabled before age 65. Disability Planner, Social Security Online, 2005.

[2] Also unless you personally pay premiums for your disability insurance with after-tax dollars, any benefit you receive will be subject to income tax. This applies to all employer paid plans. Therefore calculate your need for income with this in mind.

Although cost varies depending upon the type of services required and geographic location, the national average private pay cost for one year in a nursing home semi-private room is $57,670. A home health aide costs over $18 per hour. The greater demand for care of baby boomers will lead to even higher costs. Not only is it expensive, each person at age 65 has a 40% probability of needing it with women having higher demand than men. A high probability of high total expense like LTC requires financial protection through insurance.

Medicare and Medicaid will not adequately cover the cost of long-term care. Medicare will pay for up to 20 days skilled care in transition between hospital and home under limited circumstances. Medicaid pays for your care in some facilities after you have exhausted almost all of your own resources. Regular health insurance generally excludes payment for custodial care which comprises most long term care. Disability income insurance is to pay your living expenses, and is almost never sufficient to pay for long term care also and the benefit period usually ends at age 65 after which 90% of this care is needed.

Timing your purchase of LTC insurance depends on many factors. Premiums remain more affordable in your forties, fifties and early sixties, so the younger the better. You must still be in relatively good condition both financially and physically to qualify for it. But a serious accident or debilitating illness may also occur at any age, cause financial havoc and negate your chance to buy coverage for older age.

The best LTC coverage pays for care in a facility if required or for in-home services so long as you need help with two or more of the activities listed above, or have a severe cognitive impairment. Because of future inflation, it may be wise to buy as much daily benefit as you can afford, even $165 or more. A comprehensive financial planning approach will also consider the use of income from your other resources. As with disability income insurance, buy a policy that guarantees renewability as long as you pay the premiums. In order to increase premiums, the company must petition the state insurance commissioner and show its need to raise rates on all insureds similarly situated.

In addition to many choices within a comprehensive LTC contract, life insurance or annuity policies can sometimes be used to fund the LTC costs. With this much complexity, a professional LTC insurance specialist can explain the alternatives and show their price differences among several top-rated companies.

[1] Across the States: Profiles of Long-Term Care, AARP Public Policy Institute, Sixth Edition, 2004.

How Can I Protect Myself Against Identity Theft?

It's no secret: Identity theft is a growing, significant problem in America. Almost daily you can read about a security compromise at a major company or government agency. Think you're not at risk? Unfortunately almost everyone is for many reasons, including the proliferation of illegal immigrants, undocumented workers, organized crime rings, easy credit, camera phones, and the use of the Internet for financial transactions and communication. Even if you do everything you can to protect your own personal information, what about the other organizations that have your information?

Identity theft can involve much more than just your financial information and credit. Without your knowledge, thieves may change your address, obtain a new driver's license or new Social Security number, have a medical test performed, commit a crime in your name and apply for a job.

This is not an exhaustive list of do's and don'ts, but it's a good start to help you reduce your risk of becoming victim of identity theft:

1. Regarding mail and statements, do not let your mail accumulate and do not leave personal bills in your unsecured box to be picked up later. Stop your mail when you will be away form home for a few days or weeks. Mail your payments from a U.S. Postal Service mailbox. Shred your old mail and other personal information.
2. Do not put your Social Security number on your checks or driver's license. In fact, avoid providing your Social Security number and birthday unless absolutely necessary.
3. Review your credit report regularly. There are three major credit bureaus, Experion, Equifax and TransUnion. Recent federal law requires each agency to supply you with a free credit report each year. For more information, go to www.annualcreditreport.com.
4. Do not reveal personal information to anyone until you know why, how and by whom the information will be used.
5. Secure your Internet passwords and Personal Identification Numbers. Never give out your passwords on the Internet. Always use a nickname in any chat rooms.
6. Maintain all financial records properly in a safe place. Know what time of the month your statements come so if you do not receive them you can contact the company. Review each statement closely.
7. Make a list or copy the contents of your wallet so if it is stolen you will know who to notify. Then notify your bank and credit card companies immediately.

The Federal Trade Commission works for the consumer to prevent fraudulent, deceptive and unfair business practices and to help consumers spot, stop and avoid them. Also a variety of private identity/credit monitoring protection products exist for you to consider. Be sure to buy a plan that covers the adults in your family for one monthly fee and includes an identity restoration benefit. A quality restoration benefit will help reduce your out of pocket expenses and time spent away from work.

How Much and What Kind of Automobile, Homeowners and General Liability Insurance Should I Have?

Even though the laws of Missouri currently only require a minimum automobile liability insurance amount of $25,000 per person for bodily injury with a maximum of two times that amount per accident, prudence as well as good citizenship requires higher limits of coverage. The cost difference between this and $100,000/$300,000 limits are not great enough to risk harming someone else to an extent that you are not able to be responsible for your negligence. In addition, if their damages exceed your protection, you do not have sufficient time or energy to be ensnared in litigation for a long period if you can help it. Err on the high side. Being the model citizen is good, but protect yourself and family too by having high limits for uninsured and underinsured motorist coverage. If you become disabled for life by someone with only minimum liability insurance, you will have to be satisfied with just your own disability income if you did not have high enough levels of these two.

For the same reasons, make certain you have adequate liability insurance for your residence, whether you own or are renting it. The premium for liability is not expensive and you might become socially and financially embarrassed for your failure to be responsible if a friend or relative is hurt on your premises. Property and casualty agents often recommend a few thousand of medical payments coverage also because paying for someone's emergency room visit without a hassle may prevent a larger claim against you from the incident.

While on this subject, ask your insurance agent or company about Umbrella Liability insurance. This is liability protection that overlays all of your other specific coverages with greater limits to solve for the unusually high level of damages or an unusual source of liability such as your service on a charitable organization's board of directors.[1]

If you want or need to save money on property and casualty insurance, the best method is to raise your deductible levels for your own comprehensive or property damage protection. With the proper emergency fund in place, you can easily afford to self-insure the first $500 or even $1,000 of damage to your vehicle. You will definitely have to pay for your own loss once in a while, but you will save enough in premiums year after year to make it worthwhile. But guard against the big losses by making sure you have replacement values protected for your home and its contents.

[1] Homeowners and Umbrella policies generally do not protect you from professional liability. Therefore, you may want to consider a stand-alone professional liability insurance policy.

Chapter 4 Retirement Planning and Investing

Careful planning is necessary before and after retirement because conditions never remain static whether it's thinking about how inflation will result in higher prices for goods or the fact that we are living longer lives. It is a mistake not to plan carefully how we want to live during retirement. Don't be surprised that your health care, insurance and leisure expenses may be considerably more during retirement than during full-time employment. Learn as much about yourself, your finances, your family's needs, and dozens of other variables before you pull the trigger on retiring from your education career.

How is Retirement Being Redefined?

With many Americans retiring from their primary career at earlier ages, the whole concept of retirement has changed drastically. When Social Security was first instituted in 1935, age 65 was chosen for the start of payments. Most people did not live that long but if they did, they were often physically broken down and used up. Today you can enjoy relatively good health for decades after retiring.

Retirement today is often called "rehirement." Since those who quit working, sit at home and watch television all day often die quickly, retirees know that they must be productive with hobbies, charitable causes or new business ventures. You may be able to continue in the field of education on a part-time basis in Missouri. Since eight other states border Missouri you may also live close enough to teach or work full-time outside of Missouri and still legally collect your full benefit. The key to the door of multiple opportunities then is the preparation you make beforehand.

We all joke about being a greeter at Wal-Mart, but for some extroverts it would be the perfect position. Perfect, that is, as long as you don't need a lot of income. You will not only need enough income from your pension and investments, but think creatively and plan for ways you can keep contributing to your family and community whether you do it for pay or as a volunteer.

When Should I Plan for Retirement?

As the old saying goes, "a stitch in time saves nine." And, as shown on page 10, a dollar saved in your twenties can be worth sixteen or more in your mid-fifties. If you control your spending, save some money as you work through your career and finish thirty or more years in PSRS/PEERS you can make retirement preparation look easy because it can be.

Begin planning early in your career for your future after education as you strive to be debt free except for a mortgage as soon as possible. You also plan for retirement when you look ahead and properly prepare for your children's higher education. You even prepare for retirement while you teach your children the lessons of money management at young ages so you are not tempted to bail them out of financial messes when they are young adults.

Even so, you can still help yourself even if you begin planning for your retirement just a year or two prior. If you are an avid do-it-yourselfer, you can use online software to determine your readiness and piece together the effects of the pension, tax sheltered annuities and other investments. If not, get help from a professional financial planning advisor as early as possible. Remember that the biggest roadblock to retirement planning is simple PROCRASTINATION.

When Can Or Should We Retire?

Retirement will depend largely on financial assets, health, desire and perhaps emotional readiness. Ideally we should plan on retiring after 30 or more years of full-time work experience unless health, family situations or other unforeseen circumstances dictate otherwise. Every retirement system has specific requirements for taking a full or reduced retirement pension and provides for early retirement. Pay close attention to your pension plan details because it will be the foundation on which your retirement success is built!

Many of us spend years planning for retirement. Others spend more time planning an extended trip than their own retirement. Some people are anxious to retire so they can lighten up on their responsibilities and enjoy more leisure time. In case you haven't noticed, it costs a lot to play and travel, so plan accordingly. Some do not get to enjoy choosing their date of retirement. There are no guarantees in life except one. Regardless of whether we plan for our retirement or not, a sudden accident, illness or general poor health can spoil the best laid retirement plans.

Many people have mixed emotions about retiring. Some educators cannot wait to change, but others love their work and want to continue to do what they enjoy most. If you still see each day as a fulfilling adventure, you should probably continue where you are. This applies even if you have your financial affairs in order. Money is not the only thing and does not even need to be the main thing.

Regardless of your level of anticipation, make sure you have plenty of enjoyable activities to pursue after retirement or you could end up having reservations about why you ever stopped working at your full-time job. Other important considerations along this same line include the following:

- Relationships with work colleagues may change or end when you retire.
- Important professional responsibilities are reduced or eliminated.
- Professional growth opportunities must be pursued on your own.
- Adjusting to more leisure time.
- More time to spend with one's spouse and family.

Your real age is more than a number. Our retirement years may start in our 50's or later. Regardless of when we retire, we may live decades longer. Staying active and giving back to our church, friends, colleagues and communities is important. If you are so inclined, start by looking into volunteering opportunities in your area.

If you find from your planning diagnostics that you will not have enough income to fulfill your needs or desires for retirement income, you may be very unwise to go ahead and leave your district's employment just because your thirty years have passed. Consider whether other job opportunities will pay as much as your current salary plus your existing benefit package. Do not forget to include the 100% employer match you receive to your mandatory contributions. Your retirement income will grow because of the higher totals in the formula and because you have a slightly shorter retirement period statistically.

If you also work in the private sector it is likely you will have several employers or even different careers. This increases the probability that you will have more than one type of formal retirement plan during your working years. Most private employers do not provide a defined benefit retirement plan for employees. They may offer a defined contribution plan, thus requiring employees to make their own retirement contributions. With a defined contribution plan, such as a 401(k) plan, if your employer matches your contributions up to a certain point, be sure you contribute up to that point in order to take advantage of the full employer contribution. As an example, if a private employer will match one-half of your contributions up to 5%, you will automatically start with a return on investment of 50%.

Because of the varying types of private pension plans, it is very important to not make snap decisions when you leave one job for another. Monies may be best left in place, transferred to a self-directed Individual Retirement account, or any number of ways that will be in your best interest. Once again, consult your tax or financial professional to assist you with your planning. If you simply take your money from a retirement plan in cash to pay bills or for "wants" you may be sadly surprised to find that taxes will gobble up a large percentage of your funds.

What Is Unique About Women and Retirement?

First of all, women make up more than 75% of our Missouri classroom teachers *(Recruitment and Retention of Teachers in Missouri Public Schools: A Report the General Assembly*, December, 2001).

Second, since most women live longer than men, they will likely be retired longer than men. The average age for widowhood is 56 and the probability of this change in status means that women often must make certain that their spouse maintains sufficient life insurance to make up for any shortfall in retirement assets. The possibility of becoming divorced and receiving an unfavorable division of the couple's assets must also be considered.

Third, women on average earn less than men over their working careers. Many women take significant time off from careers to raise children. Women also bear a greater share of the burden of caring for aged parents than men. Finally while this is hopefully changing, women traditionally have not been expected to be as knowledgeable and involved in investments and financial planning. These factors make extensive retirement planning even more critically important for women.

What Are Special Retirement Considerations of Baby Boomers?

Boomers (those born from 1946 through 1964) make up over one-quarter of our country's population. Boomers are unlike older generations both in lifestyles and attitudes. Boomers have lived their lives in relative prosperity and often desire a standard of living that is above their means. Therefore borrowing has been a hallmark of their financial lives. A continuing high level of debt will have a tremendous impact on their ability to retire when they want to and pay for the goods and services they desire.

Being so demographically significant, Boomers will now face shortages and higher costs for healthcare, senior housing and long term care, just as they experienced with automobiles, education and housing in their younger years. The inflationary pressures in these industries are likely to be tremendous. Consequently there may be a dramatic change in the demand for personal services relative to consumer goods. As the quality of healthcare technology increases, the sheer explosion in demand for it promises to make some form of rationing in services likely.

Boomers have been more likely to have multiple employers than their parents, often leading to lesser retirement plan balances. Their divorce rate has been higher and personal savings rate lower than their parents'. These facts point to a strong possibility that many Boomers will be working well into their 60's and 70's in order to continue their more expensive lifestyles. The wildcard from family to family may be the level of inheritance from their more frugal parents.

Speaking of parents, Boomers currently experience a high likelihood of feeling "sandwiched" between the demands and responsibilities for caring for aging parents and children or grandchildren at the same time. This tension may also lead to higher levels of part-time employment or more flexible duties that last until older ages for this generation. At the least, trends emphasizing pay for productive results or outcomes in place of hours spent "on the clock" (along with working from home) should continue to grow.

Chapter 5 Educational Planning and Investing

What are the best Plans for Education Savings?

There are several good options for college funding. The best methods involve tax-advantaged savings programs as well as personal savings. A few years ago, the federal government added Section 529 to the Internal Revenue Code that allowed states to sponsor special educational savings plans. Missouri's M.O.S.T. Plan is the only college savings program which affords Missouri residents a state income tax deduction on the first $8,000 of annual contributions. In general, high levels of contributions per child are allowed. Even greater savings come from the exemption from future federal and state tax on all earnings on monies invested in such plans so long as they are used for qualified educational expenses. These include expenses for elementary, secondary or higher education without age limits. If never used for such by a person in the extended family, the earnings are simply taxed at ordinary tax rates with a 10% penalty added. However plan limitations severely restrict investment flexibility.

In contrast, Coverdell Educational Savings Accounts can be established for a child permitting a full range of investments similar to IRA accounts. However federal law limits annual contributions per child to $2,000 regardless of their source. Although no income tax deduction rises from contributions, all earnings expended for a recipient's higher education by age thirty are exempt from federal and state income taxes. You can also substitute one related child for another in order to appropriately spend the account balances.

Series I Bonds and Series EE Bonds (issued by the U.S. government) accrue interest at relatively conservative rates but the earnings are exempt from income taxes when used for qualifying college expenses. There does not need to be any advance special designation of these instruments for educational use.

Likewise any adult can establish an account to benefit a minor child under the Uniform Gifts to Minors Act (UGMA) or the Uniform Trust for Minors Act (UTMA). Although there may be wide latitude involved, all of the money must be spent for the benefit of the child during minority or be made available to him or her upon reaching the age of majority under applicable state law. Earnings from such an account are taxed to the minor. However the so-called Kiddie Tax causes the earnings to be taxed at a parent's highest marginal tax rate if the total exceeds rather modest levels.

Starting early and consistently contributing to one or more college savings plans is an excellent way to invest in your children or grandchildren and give them a head start toward the cost of higher education. CAUTION: saving for future college expenses should not take precedence over saving for your own retirement. You can borrow for college expenses, but not for retirement!

Chapter 6 Investing From A to Z

We all know there are a multitude of investment vehicles, ranging from safe to risky. Will Rogers once said, "I'm more concerned about the return of my money than I am the return on my money" and, "The quickest way to double your money is to fold it." Most people realize that it is best to diversify their investments if given a sufficient amount to invest and that if they cannot afford to lose their money, they should err on the side of being conservative. However, what many investors fail to realize until too late is that inflation is the biggest obstacle to a comfortable retirement. If they are too conservative with their investments, they may even lose ground in relation to purchasing power.

Most investment vehicles fall into two categories: fixed-income and equities. In fixed-income investments we can reasonably expect to get back our principal (original investment). We are in essence loaning our money to another entity in return for a fixed, or in some cases, a variable rate of return. Examples of fixed income investments include: money market accounts, certificates of deposit, savings accounts, bonds, mortgage or asset backed securities, and other debt type securities.

Equities give us part ownership in an entity. Equities may increase or decrease in value. Stocks and mutual funds are examples of equities.

It is a good idea to start your investment strategy by building an emergency saving fund, through the use of a savings account or money market account. Most experts agree that is wise to keep three to six months of one's salary in an investment account that can be easily accessed in the case of an emergency. Once this is established, you may want to move on to saving through a certificate of deposit or bond. Bonds come in three types: corporate, government, and municipal.

Moving on down the line with your savings diversification plan, the next step may be to start contributing to mutual funds. Individual mutual funds are made up of many different investments to spread the risk so the risk of losing a large percentage of assets is less likely. Investing in mutual funds can be done with as little as $25 per month, which can be invested in a wide spectrum of diversified funds, such as: growth stocks, income-producing bonds, international stocks, small company stocks, and almost everything in between. There are front load, back load, and no load funds. Each has its advantages and disadvantages, so be sure to read the prospectuses, and inquire as to the specific fees and regulations. This is where the advice of an experience financial advisor can be a real time saver and help to your understanding.

As you become more experienced in the investment world, you may want to try trading individual stocks. This is where the large returns can be made … or lost. Others may feel like dabbling in real estate, commodities, collectibles, precious metals, antiques and so forth.

As we approach retirement, we often want to invest more conservatively in annuities, U.S. government securities and other fixed income-producing investments. But keep in mind that you should stay diversified in some equities as a hedge against inflation to prevent a subsequent loss of purchasing power. If it were not for inflation and health care expenses, figuring out how much you need to retire on might be a little easier.

What Are Some Investment Principles?

Diversification: Our parents and many of our teachers probably taught us that we shouldn't "put all of our eggs in one basket." No one type of investment will always be the top performer. Therefore, over time, it pays to diversify into different investments, equity and fixed, with assets spread over a broad range even within these categories. Historically, over a long period of time, equities have outperformed fixed investments.

Allocation: Allocation refers to how we allocate or structure our investments in different asset classes. This will depend on our objective, risk tolerance, and time horizon before we will need to use the assets. There are models of allocations which can change with time and age. We can usually afford to take more risk the younger we are, because of the time available to recover. As most people approach retirement, they become more conservative with their investments, because they know they will likely be using them in short order.

Re-Balance and Re-Allocate: One may need to re-balance his portfolio depending on the markets and their objectives. This usually occurs when one or more asset classes grow at a faster rate than the others, thus putting his overall portfolio out of alignment with his current risk tolerance and investment objectives.

Dollar-Cost Averaging: This is a smart strategy to use when you invest over a long period of time. With dollar cost averaging you are investing a consistent amount each month. Although the price per share will fluctuate from day to day, you will be buying more shares when the price is low, and fewer shares when the price is high. This ensures you are buying at the high, middle, and low ends of the specific equity price spectrum. This is a common way to invest in mutual funds.

Laddering: Laddering is a strategy used to buy certificates of deposit and bonds so that they mature at different times. This can help to alleviate the problem of one's fixed interest accounts having to be all reinvested at a time when rates are abnormally low.

Liquidity and Marketability: Use your common sense with these two terms. Unless we know we will never need to use our assets, passing them on to future generations, we need to know how liquid and how marketable our assets are. The farmer, who owns 1000 acres of land during a prolonged drought, may not be able to sell the farm at a decent price. The farmer who owns 1000 acres sitting on top of a nuclear waste site, may not be able to sell it at any price.

Leverage: Leverage is often used to own and control assets with an investment much less than the value of the controlled asset. Real estate investments often use this principle.

Compounding: This is a powerful technique to let money grow over time. Interest earnings are returned to the principal amount to compound again and again. See page 5.

Tax Efficiency: Tax efficiency can be an important consideration with investments. Earnings from a Roth IRA, or municipal bond are tax-free. Qualifying dividends and capital gains (until 2008) are currently taxed at 15% on the Federal level, rather than a person's top personal tax rate.

Tax Deferral: Tax deferral may allow you to defer income into a later tax year, or into retirement when your income, or tax rate may be lower.

How Can We Manage Investment Risk?

Investment Risk: One of the greatest truths of the investment world is that risk and reward go hand in hand. The greater the risk, the greater the "potential" reward. We need to balance our own risk-reward equation to meet our own philosophy, age, and resources.

Market Risk: In simple terms, market risk can be defined as the possibility that downward changes in the market price of an investment will result in the loss of principal for an investor. Market risk is most closely associated with the ups and downs of the stock and commodity markets.

Credit Risk: This is also known as default risk, or the chance that the issuer of a bond or other debt-type instrument will not be able to carry out its' contractual obligations and pay you back your full initial principal investment.

Interest Rate Risk: If interest rates rise, you have interest rate risk if you own a fixed rate investment that doesn't mature or change rates until some time in the future. As interest rates rise, bond prices tend to fall, and vice versa.

Call Risk: A municipal security may be prepaid, or "called" before the maturity date, if interest rates are falling. Make sure you know the call provisions of any bonds you purchase so you can better anticipate the call risk you have, as it relates to lower than anticipated interest earnings.

Tax Rate Risk: This refers to the possibility that a change in tax laws may change the tax status of a particular investment, or on the rate of taxation of deferred income.

Inflation Risk: Inflation risk is the risk that you may lose purchasing power on your assets, compared to what other assets cost. If you are not aggressive enough with your investments, you could end up losing ground. From a historical perspective, inflation has averaged over 3% the past 25 years.

Foreign Investment Risk: Investments in foreign securities involve risks related to political, social, economic, liquidity, money rates, and volatility. Remember, these risks are also present in the U.S.

How Much Risk Are We Willing To Take With Our Investments?

Surveys show the answer to this question depends largely on the investor's age. Younger generations are willing to take greater risks for greater gains. 45% of generation Y (those born in 1977 and later) and 48% of generation X (those born between 1965 and 1976) are willing to take substantial risk with their investments. This compares with 36% of Baby Boomers (those born between 1946 and 1964) and the silent generation (those born before 1945) prefer average risk for average gain.

When it comes to financial goals, all age groups cite retirement planning as a primary goal. Younger generations are more likely to save for educational expenses, a house or other large item. Older investors are more likely to seek income-producing investments and those that decrease their taxable income.

What are Stock Indices, Capitalization and Benchmarks?

The various stock markets in the United States are measured by indices. A stock market index is a subset of stocks within the overall stock market created to measure the performance of the stock market as a whole or a segment of the market. The most commonly known index is the Dow Jones Industrial Average (DJIA). The DJIA measures the stock performance of the 30 largest companies in the United States. Because of the limited scope of the DJIA, it is not the best overall indicator of the stocks in general.

The Standard and Poor's 500 Index is a better measure of the entire U.S. stock market because it tracks the largest 500 companies. The Wilshire 5000 is the broadest stock market index. It actually encompasses all U.S. stocks, about 7,000 now.

The NASDAQ Composite contains all foreign and domestic corporations listed on the NASDAQ market (sometimes called the Over The Counter or OTC Market) totaling over 5,000 companies. The NASDAQ has become the primary stock market for technology companies with approximately 70% of the value of the index being comprised of technology stocks. The NASDAQ 100 contains the largest and most actively traded 100 stocks in the NASDAQ stock market.

The Russell 2000 was created for investors to track stocks from smaller companies commonly referred to as small cap stocks. The Standard and Poor's Small Cap 400 comprises 10% of the total market. The EAFE index tracks stocks in foreign companies in developed countries such as Great Britain, Germany, Ireland, France, and Singapore.

The most common way to characterize stocks is through their market capitalization. To determine a stock's market capitalization, multiply the price of a single share of stock by the number of stocks held by investors. The typical classification of stock companies is:

- Large Cap = $10 billion or more of market capitalization.
- Mid Cap = $2 to $10 billion.
- Small Cap = $1 to $2 billion.
- Micro Cap = $1 billion or less.

Mutual Funds measure the performance of their funds based on the type of shares held in their portfolio compared to the performance of the indexes. If you own stocks and/or mutual funds, it is a good idea for you to make your own comparisons as well.

Chapter 7 Legal Issues

Is Our Legal House in Order?

Titling (the legal listing of ownership) of property and asset accounts is very important. We don't often realize the consequences of improper titling, because it doesn't affect us until we die, and our loved ones have to sort things out. One of the biggest mistakes made is not keeping a beneficiary designation up to date. If there is a death or change in marital status, and a beneficiary designation is in place that we aren't happy with, it can't be changed after the fact. A beneficiary designation on an insurance or investment account will take precedence over one's stated wishes in a will.

There are several forms of ownership. Each type has advantages and disadvantages.

Sole Ownership: This means there is only one owner.

Joint Tenancy: Is when property is owned by two or more people.

Joint Tenancy With Right of Survivorship: This means that if one owner dies, the other owners assume complete ownership.

Tenants in Common: This is where two or more people own property, but without the right of survivorship. Instead, at the death of one co-owner, his or her interest passes to whoever is named in that person's will. If there is no will, state law dictates which of the deceased person's heirs inherit the property.

Community Property: This is a special form of joint tenancy between a husband and a wife. Each spouse owns half of the property bought in the marriage. Then, either spouse can will his or her share of the property to anyone they want.

Tenants by Entirety: About half of the states, including Missouri, recognize the special ownership right available to married people. Each spouse owns half of the property. Neither spouse can sell the property or transfer ownership of the property without the consent of the other spouse. If one spouse dies, the surviving spouse is entitled to all of the jointly owned property.

Cautions. Be careful about adding someone to a title because it can cause serious tax and legal consequences. Property held jointly is subject to claims by creditors of the owners. For example, if a couple added a child's name to their home title, and that child is at fault in an accident, or has financial problems, the home could be subject to the lawsuits and liens of other parties. Using a will or trust to make sure your wishes are realized is a safer way to pass property on to a child. Although you may think there are good reasons to transfer property to someone else, this could cause unintended tax consequences to the recipient, and in all cases causes you to lose total control over the asset. Once you give, it's totally up to the recipient as to whether they keep you on their giving list. Currently, an asset which passes to someone upon the death a loved one or friend, receives a stepped-up value to the current market value on the asset. If the asset is passed while the giver is still alive, the asset doesn't receive the stepped-up basis, which could create a much higher tax bill if the asset is sold. It is always wise to seek the advice of a qualified attorney, and/or tax specialist, for these types of matters.

Many people don't plan ahead for the "what ifs" of becoming totally incapacitated, or even mentally incompetent, but it happens thousands of times a day in our country. Don't put off until tomorrow what you need to do today. Without a power of attorney, if we become incapacitated, our loved ones may not be able to make medical and financial decisions for us without great expense and mental anguish. Not long ago, the Terri Shiavo "Right to Live" case was a prime example of how a family can be torn apart when our wishes are not captured on a legally binding document. As with much of our planning efforts, you plan because you love those who care for you, not because you are trying to take care of your own needs.

Power of Attorney: This is a document that authorizes another person to act as if they were us. This person is called our agent, or attorney in fact. This can be broad or limited, depending on the nature of the need. A simple power of attorney expires when we become incompetent. In that case, someone would have to be designated as our guardian by order of the court.

Durable Power of Attorney: This stays in effect even when we become incompetent or incapacitated. A durable power of attorney can be either immediate, or springing to become active. A springing durable power of attorney would need to be triggered by a medical declaration that we are unable to handle our own affairs. A durable power of attorney will not suffice for someone to make health care decisions on our behalf.

Durable Power of Attorney for Health Care: This allows us to appoint an agent to make health care decisions for us, if we are unable to do so for ourselves. The ultimate decision, in this realm, is the decision to take someone off life support. This document gives someone other than health care providers the decision making power, but only after the health care provider makes the determination that we are no longer able to make our own decisions.

Health Care Directive: This sets forth our wishes about health care issues, and is sometimes called an advanced directive, or living will. An example of issues set for the in a health care directive could include withholding or withdrawing life prolonging procedures, and what types of treatments we object. This document is extremely important to family and doctors, as was recently demonstrated by the nationally publicized case of Terri Shiavo.

Anatomical Gifts: We can authorize the donation of our organs by signing the back side of our driver's license and having two people witness our signature. We should also discuss this with our family and loved ones.

Chapter 8 Additional Resources and Suggested Readings

These websites, organizations, and publications have more information on financial matters:

- **Retirement Plans**
  - http://www.psrs-peers.org (Public School and Education Employee Retirement Systems of Missouri)
  - http://www.dol.gov/ebsa/consumer_info_pension.html

- **Financial Calculators**
  - www.ssa.gov/planners/calculators.htm

- **Common Sense Finance**
  - http://www.moneymanagement.org Money Management International
  - http://www.daveramsey.com Dave Ramsey: The Total Money Makeover
  - http://www.suzeorman.com Suze Orman: Young, Fabulous & Broke
  - The Guide To Understanding Consumer Insurance Products: How to select the tools to accumulate wealth and safeguard your home and retirement, by A.M Best Company, http://guides.ambest.com/#ConsumerGuide

- **University of Missouri Extension Programs**
  - http://extension.missouri.edu/hes/money.htm

- **Retirement Planning for Adults**
  - Kiplinger's: Retire Worry-Free
  - The Wall Street Journal: Guide to Planning Your Financial Future
  - Retirement Bible, by Lynn O'Shaughnessy
  - Left-Brain Finance for Right-Brain People: A Money Guide for the Creatively Inclined, by Paula Ann Monroe
  - Retiring Well, by Hope Egan, Matthew James and Barbara Wagner

- **Retirement Planning for Children & Young Adults**
  - Missouri's 529 College Savings Plan https://missourimost.s.upromise.com/
  - The Basics of Saving and Investing: Investor Education 2020, by The Investor Protection Trust, www.investorprotection.org
  - http://www.kidsfinance.com/
  - http://www.richdad.com/
  - National Endowment for Financial Education, www.nefe.org

- **Legal, Life and Financial Planning**
    - Missouri Bar Association, www.mobar.org
    - Life Choices: Communicating About the End of Life, www.ago.mo.gov
    - Life Insurance Needs and Human Life Value Calculator, www.life-line.org
    - Disability & Long-Term Care Insurance, www.life-line.org
    - Medicare, www.medicare.gov
    - Understanding Taxes, http://www.irs.gov/app/understandingTaxes

- **Identity Theft, Fraud and Consumer Protection**
    - Federal Trade Commission www.ftc.gov
    - Missouri Attorney General www.ago.mo.gov

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Help A Teacher -
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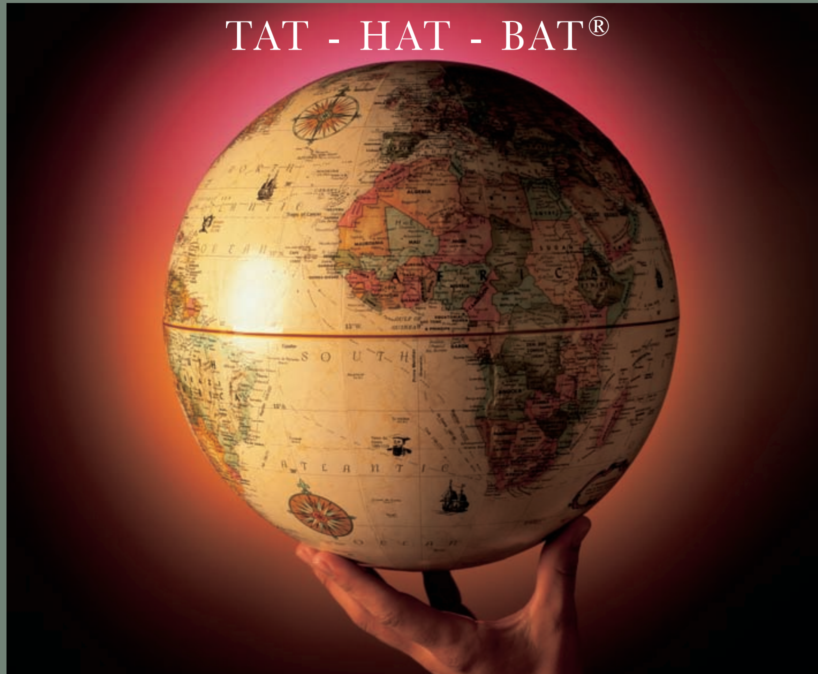

www.lifelongteachers.net

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