Briefly Noted

10 Tips for Getting More out of Your IRA

The effectiveness of an individual retirement account (IRA) can be maximized through a combination of strategic planning and careful decision-making. MarketWatch.com columnist Robert Powell relates strategies in particular that professionals say investors should consider implementing.

Those strategies are:

1. **Consolidate Accounts:** If you have multiple accounts, consolidating them can help you avoid (or at least reduce) maintenance fees, simplify your record-keeping and give you a clearer picture of your investments.
2. **Pay Attention to Allocation:** Review your investments to ensure they match your allocation goals. Also, place your least tax-efficient assets, such as corporate bonds, in your tax-deferred accounts.
3. **Tax Diversify:** Use both a traditional and a Roth IRA to reduce your tax bill and give you more flexibility over the amount and timing of withdrawals.
4. **Convert to a Roth IRA:** Consider converting to a Roth IRA to better manage your aftertax income.
5. **Fund Both an IRA and a 401(k):** Retirement savings can be boosted if contributions are made both to a 401(k) retirement plan and an IRA.
6. **Use Catch-Up Contributions:** Investors age 50 or older can contribute up to $6,000, depending on their income, to an IRA or Roth IRA.
7. **Fund the Non-Working Spouse's Account:** Couples who file joint returns can contribute up to $5,000 ($6,000 for a spouse age 50 or older) into the non-working spouse's account. This means married couples could contribute up to $12,000 per year, subject to age and income requirements.
8. **Withdraw From the Right Account:** After taking the required minimum distribution (RMD), take money out of your taxable accounts before touching your IRA accounts.
9. **Leave a Legacy:** Consider leaving tax-qualified assets to a charity.
10. **Consider Inheritance:** An inherited or beneficiary IRA can provide tax and monetary benefits to your heirs.

Source: "10 Ways to Get the Most Out of Your IRA," by Robert Powell, MarketWatch.com, February 21, 2012.

Life Spans, Health Care Costs and Rethinking Retirement

Three out of four affluent Americans would change how they approach money management if they knew they would live to be 100, according to the Merrill Lynch Affluent Insights Survey. Respondents said they would continue working at least part-time and/or re-evaluate their saving and investment strategies if they knew they would become centenarians.

The survey asked more than 1,000 individuals with investable assets of $250,000 or more about their goals and concerns. Many respondents cited the uncertainty of longevity and health care costs as key challenges to their investment strategies. Rising health care costs were cited as a top concern by 79% of respondents. Sixty percent were concerned about ensuring they have enough assets to last throughout their lifetime.

Many respondents said they do not expect to have a source of lifetime income beyond what is supplied by Social Security. As for pensions, just 38% of those under 50 anticipate or currently recieve a pension (versus 57% for those over age 50).

Respondents appeared willing to redefine traditional retirement. Nearly four in 10 would continue to work at least part-time in retirement if they knew they would live to age 100. More than 50% of respondents who had yet to retire planned on either cycling between work and leisure or working in a job they enjoy more (part- or full-time). Just 14% of respondents over the age 50 said they would retire once they hit a certain age.

Notably, providing for children and other family members was a priority. Only one in four respondents said they would be willing to leave a smaller inheritance to ensure they had enough assets to sustain them throughout retirement. Similarly, only 15% of respondents who were planning to retire in the next five years said they would be willing reduce financial support to their adult-age children in exchange for boosting their retirement savings.

With average life spans increasing, it is becoming more important for investors to consider that they could live longer they originally anticipated. This means planning for both near-term and long-term needs.

Source: "Merrill Lynch Affluent Insights Survey," February 22, 2012, Merrill Lynch Wealth Management.

Target Date Funds Misunderstood

A new survey by ING revealed gaps in investor understanding of how target date funds are designed, how they are managed, and what they are designed to do. The survey interviewed 540 defined-contribution plan participants. Within this group, 212 invested in target date funds and 328 did not.

A target date fund provides exposure to a variety of assets, most notably large-cap stocks and bonds, and adjusts its allocation as it approaches a specified date (e.g., 2020). These funds are designed to give investors a simple option for reaching their long-term goals. Their management styles and allocation strategies can very widely, however, with some funds designed to make an abrupt shift in allocations at the target date (the "to" approach) and others designed to make a gradual change (the "through" approach). Hence, the opportunity for misunderstanding and confusion about these funds is high.

An example of the confusion concerns controlling risk. More than 70% of all respondents (79% of target date fund users and 71% of non-users) said they wanted stronger protection from investment losses. Yet only about half (55%) knew a target date fund's allocation was designed to become more conservative over time. Worse yet, just 44% thought the allocation would be automatically changed over time. And just 53% were confident they would reach their retirement goals. (Among respondents who did not use target date funds, the percentages were even lower.)

The confusion extends to portfolio allocation. Both target date fund users and non-users thought diversification is important, with more than 80% of all respondents indicating an interest or strong interest in diversification. However, less than-two thirds (63%) of target date fund users believed their funds held a diversified mix of stocks and bonds. This may partially explain why 47% of target date fund users thought they needed to own other funds to obtain more diversification.

A target date fund can play a role in a portfolio if an investor understands the fund's investing and allocation strategy. Specifically, investors need to read the prospectus to learn how the allocation changes over time and what happens after the target date is reached. It is also very important to find out if the allocation will continue to evolve after the target date and at what point the fund will be liquidated or folded into another fund.

Source: "Participant Preferences in Target-Date Funds," ING Investment Management and ING Retirement Research Institute, February 2012.

From the Bookshelf

Yale economics professor Robert Shiller both defends the financial sector and offers suggestions for how it can be improved in "Finance and the Good Society" (Princeton University Press, 2012).

If Shiller's goal was to provoke thought and discussion, he has done so. He defends the roles of high-frequency traders and market makers, arguing that they bring expertise and create liquidity. He also argues that people place too much emphasis on measuring wealth by currency units (e.g., dollars in one's bank account), when their focus should be what they can purchase with those dollars.

Shiller is known for his knowledge of asset price bubbles, and he continues his discussion of them in this book. He compares bubbles to "a social mental illness." Shiller further warns that they are hard to identify because changes in price-earnings ratios don't prove that bubbles exist.

This book is worth reading for its commentary on behavioral finance alone. It may anger some readers, but it does provide a different perspective on the financial markets and the characters who make it function on a daily basis.

Joshua Brown gives a skeptical, behind-the-scenes look at how stock ideas and investment products are sold to individual investors in "Backstage Wall Street: An Insider's Guide to Knowing Who to Trust, Who to Run From, and How to Maximize Your Investments" (McGraw-Hill, 2012).

The publisher of the blog The Reformed Broker relies heavily on his past experience, openly admitting, "As a retail broker, I spent a decade learning *what not to do*." He goes into great detail about how brokers are compensated and why this often hurts investors' long-term returns. He also reveals industry secrets about why men are sold to more often than women and how sales pitches are designed to either sell an investment or to get a prospective client to hang up the phone.

This book provides a great warning guide of what to look out for, as well as giving insight into how an adviser should act. It won't make you a fan of Wall Street, but will help you identify aggressive sales tactics.