

# Update



## ARE YOU READY?

### A CHECKLIST FOR THE NEW YEAR

The start of every new year brings the promise of new beginnings. It's a time to think about setting new goals and resolving to do new things. If one of your resolutions for 2008 is to find new and better ways to manage your finances and invest your money, then jump-start your efforts with the checklist that follows.

#### Increase Plan Contributions

Are you contributing as much as you can afford to your retirement plan? The more money you put into your plan now, the bigger your potential retirement nest egg. Adding as little as five or ten extra dollars per paycheck could make a big difference over the long term.

#### Make Catch-up Contributions

Your plan may allow you to make "catch-up" contributions over and above the regular contribution limit if you are age 50 or older. If possible, take advantage of the opportunity to give your retirement savings a boost.

#### Perform a Risk Checkup

Risk tolerance is your willingness to accept the risk that an investment may suffer a loss in exchange for the possibility that it will earn high returns. It's generally true in investing that the higher the level of risk, the greater the expected rate of return. You can measure your tolerance for investment risk by answering these questions: What is my age? How long do I have before I'll need the money? Can I handle investment losses? What impact would a big loss have on my future plans?

#### Rebalance Plan Investments

The goal of rebalancing is to keep your overall portfolio in line with your risk tolerance and investment objectives. Your portfolio could become unbalanced if one or more of your investments does particularly well (or falls in value). For example, if your stock investments have been doing well, they might account for a higher percentage of your portfolio than you originally planned when you decided on an asset allocation. And you may be uncomfortable with the increased level of risk.

You can rebalance by transferring money from stock funds or portfolios into other asset classes, such as bonds and cash investments. Or you can invest more of your new

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contributions in the underrepresented asset classes until you achieve the allocation you want.

#### **Look into the Saver's Credit**

When you contribute to your employer's retirement savings plan, you might qualify to claim the saver's credit on your federal income-tax return. The credit is claimed as a direct offset against taxes, so it lowers your tax bill. To qualify for a credit, your income must fall within a certain range, depending on your tax filing status. You can find out more about the credit on the IRS's website ([www.irs.gov](http://www.irs.gov)) or by talking to your tax advisor.

#### **Check Tax Withholding**

If you get a large tax refund every year, too much money is being withheld from your paycheck. You are, in essence, providing the government with an interest-free loan. To change your withholding, ask your payroll department for a copy of IRS Form W-4. (Your state may have its own form.) Remember, you should have enough withheld to avoid underpayment penalties.

#### **Create a Budget**

Keep track of where your money goes by creating a budget. Write down your basic monthly living costs — rent or mortgage payment; utility bills; insurance; college, car, and other loan payments; food; commuting; and so on. Subtract the total you spend on these recurring costs from

your monthly net pay. The difference is the amount you have left for discretionary spending and for saving. With a budget in place, you'll be better able to see how much money you can free up for saving.

#### **Take Control of Debt**

It's hard to get ahead when you're spending a lot of your income to pay down debts. Make this the year you make an extra effort to pay down as much of your consumer debt as you can. In general, it's a good idea to pay the highest interest-rate debt first.

#### **Review Insurance Coverage**

Are you prepared for the unexpected? If not, make sure you have enough life and disability insurance coverage to protect your family and your finances should anything happen to you. The National Safety Council says that one in five people will be disabled for one year or longer before reaching age 65.

Working your way through this checklist will require a little time and effort on your part. But you can do it. And the rewards for you — and your finances — will certainly make it a smart use of your time.

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## **STORMY Weather**

Stock prices rise and fall every day. That's perfectly normal. In fact, you've probably noticed periods when the stock market gains for several weeks or even several months. These increases are the reason we invest in stocks in the first place. However, prices can also fall, sometimes for extended periods. Knowing what to do — and what not to do — during difficult times in the stock market can help you manage your retirement investments.

#### **DON'T COUNT PAPER LOSSES**

Any losses your investments suffer during market declines are only "paper losses" until you sell the investments to switch with other investments (or to take a cash distribution). As long as you continue holding an investment, you haven't lost money yet. Your portfolio may be able to recover from its paper losses over time.

#### **DON'T BE CAUGHT ON THE SIDELINES**

Selling your stock investments during down periods could potentially do more harm than good. Past market declines have often been followed by periods of price gains. You won't be able to benefit from potential upswings in the market if you have moved out of stocks and are sitting on the sidelines.

#### **LOOK AT THE LONG-TERM RECORD**

Investing for retirement is a long-term goal. Although there are no guarantees, no other asset class can match the potential of stocks to provide inflation-beating returns over the long term — despite periodic downturns (see accompanying graph). That should help you maintain a long-term view of investing when the market is falling.

## KEEP YOUR PORTFOLIO DIVERSIFIED

While it's true that stocks have a track record of long-term growth, don't overlook the other types of investments your plan offers. Diversification\* simply means that you invest your plan money in a range of investments in several different asset classes (stocks, bonds, and cash equivalents). Then, if one investment type loses value, the others may gain or hold steady. This time-tested strategy can help you manage investment risk in your portfolio.

## STAY FOCUSED ON YOUR GOALS

Don't let market ups and downs make you lose sight of why you are investing — for a financially secure retirement. By focusing on your goal, you'll be more likely to make the right moves when the investment climate is stormy.

*\*Diversification does not ensure a profit or protect against loss in a declining market.*

## SHORT-TERM STOCK MARKET VOLATILITY VERSUS LONG-TERM RETURNS

Annual Return\*

1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
33.40%	28.58%	21.04%	-9.11%	-11.87%	-22.10%	28.68%	10.86%	4.93%	15.78%

**Average Annual Total Return 1997-2006 : 8.42%**

*\*Measured by the S&P 500 Stock Index, an unmanaged index of the stocks of 500 major corporations. You cannot invest directly in an index. Past performance is no guarantee of future results. Sources: Russell Data Services and NPI*

## Get Ready To Test Your Retirement Planning Smarts

Retirement planning starts with your first contribution to a retirement account and continues throughout your working years. But how much do you really know about it? Find out by taking our quiz. Answers follow each question, but don't look ahead!

1. Shana and Doug both began working at Sooper Dooper Company at age 25. As soon as she was eligible, Shana started contributing \$200 a month (\$2,400 a year) to the company's 401(k) plan. She continued contributing until her retirement at age 65. Doug waited until he was 40 to begin making contributions. Then he contributed \$400 a month (\$4,800 a year) — twice as much as Shana — until he reached age 65. Their investments earned a hypothetical average annual return of 7%,\* compounded monthly.

Who had more money at retirement, Shana or Doug?

**Answer:** *If you chose Doug, you're off the mark by approximately \$202,000! Shana's much earlier start gave her two huge advantages: time and the power of compounding (earning income on your original investment and on the earnings it generates). Although she contributed less than Doug — \$96,000 compared with Doug's \$120,000 — Shana had \$528,025 saved at retirement, while Doug had only \$325,919 (before taking income taxes into account).*

2. After working at Sooper Dooper Company for 20 years, Soco, Huong, and Calvin were all leaving for other

jobs, so they had to decide what to do with the money in their retirement plan accounts. Soco elected to leave her money in Sooper Dooper's 401(k) plan. Huong requested a trustee-to-trustee transfer of his account balance to a rollover IRA (individual retirement account). And Calvin withdrew all his savings in a lump sum so he could pay off his debts.

How did their choices impact their federal income taxes?

**Answer:** *Soco's decision to leave her money in her current plan meant that her savings continued to grow tax deferred until she withdrew her money at retirement.*

*And because he rolled over his account balance to an IRA, Huong's retirement savings also remained tax deferred. If allowed, Huong could also have avoided taxes on the distribution by rolling the money into his new employer's 401(k) plan.*

*By taking a lump-sum withdrawal, Calvin received only 80% of his account balance — 20% was withheld to prepay income taxes. And, in his tax bracket, this wasn't the extent of his tax liability. Plus, since Calvin was under age 59½ and wasn't eligible for an exception, he had to pay a 10% early distribution penalty. Calvin not only wound up with a lot less money than he'd planned on having to pay down his debts, but his retirement savings were also wiped out.*

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3. Since their employer doesn't offer a retirement plan, coworkers Jack and Helena decided to open IRAs. Jack chose an IRA that allows him to make tax-deductible contributions and enjoy tax-deferred earnings. He won't pay taxes until he withdraws his money. Helena's contributions to her IRA are not deductible. However, she can withdraw her contributions tax free at any time, and withdrawals of earnings will also be tax free after she's reached age 59½, as long as she's met a five-year waiting period.

Which type of IRA — traditional or Roth — are Jack and Helena each investing in?

**Answer:** Jack is investing in a traditional IRA; Helena has a Roth IRA. Both offer tax advantages — Jack's is immediate since he gains a tax deduction for his contributions, whereas Helena's will be realized later when she takes tax-free withdrawals. But, unlike Jack, Helena won't be required to take annual minimum distributions from her IRA after she reaches age 70½.

*\* This example is for illustrative purposes and is not representative of any particular investment vehicle. Your investment performance will differ.*

## Keep Your Retirement Out of Jeopardy

The category is "Retirement Plans" and the clue is "Summary Plan Description." What is the question? Give yourself an A if you said "What is the short, more readable summary of a retirement plan document called?"

Saving for retirement isn't a game. You may have to rely on your own savings to provide a large portion of the income you'll need in retirement. If you're not familiar with how your retirement plan works, you may not be able to make the most of a valuable savings opportunity.

### READING REQUIREMENT

Start expanding your knowledge by reading your Summary Plan Description (or SPD). It covers the basics and has a wealth of important information. If you have any questions or concerns, contact your plan administrator (listed in the SPD). If you can't locate your SPD, contact your employer.

### STUDY GUIDE

You don't have to understand the finer points of all your plan's features. But you should have a good grasp of the basics.

**Contributions.** If you contribute to a retirement savings plan, you should know how much you can contribute. If your employer makes contributions on your behalf, you

should know how long it takes for them to become fully vested (which means you have earned the right to those benefits without the risk of forfeiting them).

**Benefits.** You should know how and when benefits are distributed and in what form. If you're in a defined contribution plan, such as a 401(k) plan, you should know what your options are if you change jobs.

**Investments.** Many retirement savings plan participants direct their own investments. If you have this option, find out how to get information about your investment choices and how to make changes to your portfolio.

### CONTINUING EDUCATION

When you receive information from your retirement plan, read it promptly. File notices announcing plan changes with your other plan documents. Benefit statements should be reviewed to make sure the information is correct. Make sure your beneficiary designations are up to date and always inform your plan administrator of any personal changes, such as a marriage, divorce, or change of address (especially if you have benefits with a former employer).

Joining your employer's retirement plan was smart. Learning how to make the most of it is smarter still.



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