Letter from the Authors

Why did we spend the time to write this guidebook? Why do we like to work with Law Enforcement Officers and Firefighters? Why do we conduct our business the way we do?

We could probably ask you some of the same questions. Why do you run into burning buildings, pursue armed suspects, go to court, or public meetings (the last two being the most dangerous)?

Our answer can be explained using Lt. Colonel Dave Grossman's *On Combat*. Grossman relays a story from a Vietnam vet and retired colonel, who basically suggests that most people in society are 'sheep.' Kind, productive, and gentle, sheep only hurt each other by accident. Given the murder rate is 4.7 per 100,000, it's a reasonable hypothesis to make. 'Sheep' is not derogatory, but complimentary. Sheep are peaceful, good creatures without a capacity for violence or danger.

Then there are wolves. The wolves feed on the sheep without mercy. They are evil men who are capable of evil acts, like murder or arson. Wolves have a capacity for violence and danger but lack regard for fellow citizens.

And then there are the sheepdogs. The sheepdogs protect the flock and confront the wolves. Sheepdogs can embrace danger and uncertainty with a deep love for their fellow citizens. As Law Enforcement Officers and Firefighters, you are sheepdogs. You serve to protect the flock from danger.

We see similar uncertainties and dangers with money. Not the kind of danger that you face, but the danger of a financial crisis affecting your family, being steered into bad investments, or losing wealth. We think you, our sheepdogs, could use a financial sheepdog of your own, someone to look out for you and what you work for, your family.

In 1989, our firm of professional advisors chose to specialize part of our practice on the financial needs of Law Enforcement Officers and Firefighters. We learned everything we could; studied the tax laws, the investment options, the nuances of family estate planning. We also studied sheepdogs to see how they tick. Not to our surprise, they tick like we do. We decided that Michigan Law Enforcement Officers and Firefighters deserve a fee-only fiduciary to look after them and their family—not someone paid on commission.

This is why we continue to write our series of *Guns & Hoses* books. We want you to be well equipped for your retirement and financial future. We want your family to be financially safe. What's the catch? We think doing a great job for you might encourage you to hire us to work for you someday. More importantly, we think it's the right thing to do. In the end, there is only one thing to do—the right thing.

Thank you for your service,

Leon & Matthew

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Introduction

This guide is written to help Law Enforcement Officers and Firefighters plan for their retirement. As a first responder, you have some issues to consider in retirement. These include understanding what a Deferred Comp plan is and how it is different from a Defined Benefit plan, how to invest your Deferred Comp plan with the same strategy pension plans are invested, and how to withdrawal from your plan upon retirement.

We've been working with Michigan first responders for over 27 years. We think Law Enforcement Officers and Firefighters deserve good unbiased advice from professionals who look out for them and their family, and aren't necessarily trying to shoehorn a product into the their plan. In fact, we don't sell products. We're a Registered Investment Advisor, independent of any other company; we work for our clients and our clients alone. Our goal is simply to serve our clients with good, solid advice on their benefits, taxes, investments and estate.

Some questions we will address in this guide include:

- How to build an investment plan for your retirement
  - How to build a mix
  - How to set your investment policy
  - Why fees matter
  - Why trying to time the market may not work
- The best ways to take withdrawals
  - Which vehicle has the least taxes
  - When Roth IRAs make sense
- How to name the proper beneficiaries
  - Why you should have 'three layers' of beneficiaries
  - Why you shouldn't name your estate as a beneficiary
  - The right way to write a beneficiary designation

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Guns & Hoses
Deferred Compensation & Defined Contribution Guide for Michigan Law Enforcement Officers and Firefighters

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LJPR Financial Advisors

Michigan Law Enforcement officers and Firefighters have a wide array of benefits unique to their profession. These range from the nuances of annuity withdrawals in certain Defined Benefit pensions to DROP plans and the aspects of Social Security benefits in exempt systems. This guidebook is intended to cover some of the issues surrounding two types of Defined Contribution plans: Deferred Compensation plans (Deferred Comp or §457) and Defined Contribution pensions (DC or §401(a)). Virtually all Law Enforcement Officers and Firefighters have access to a Defined Contribution or Deferred Compensation plan.

A Note about Terminology: For purposes of this guidebook, we will use the acronym "DC" to mean a Defined Contribution pension plan (401(a)) where the employer and the employee make contributions. We will use "Deferred Comp" to mean a Deferred Compensation plan (§457) where the employee makes voluntary contributions. Both could be abbreviated "DC," but in the pension world DC means the 401(a), and Deferred Comp means the §457.

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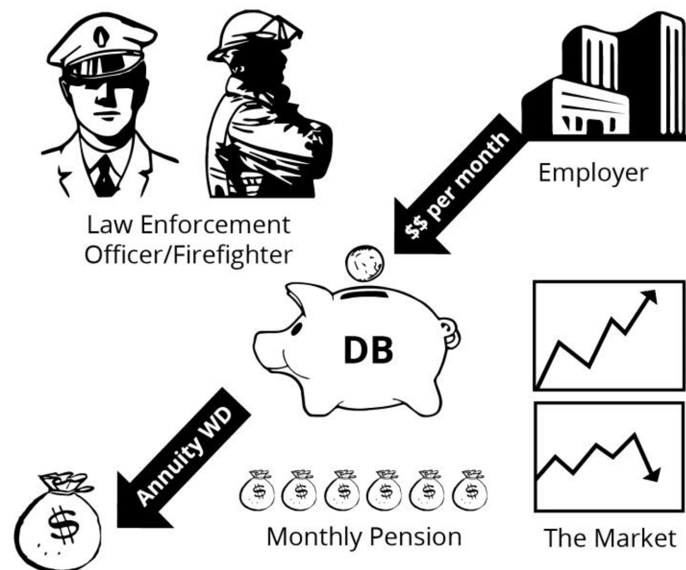
Chapter 1
Deferred Compensation Plan (§457) Guide for Michigan Law Enforcement Officers and Firefighters

Basics: What is a Defined Contribution plan? It's important to note that both Deferred Comp §457 and DC 401(a) plans are both Defined Contribution Plans. The major difference is that the **Deferred Comp** plan is strictly employee contributions and completely voluntary. On the other hand, a **Defined Contribution** plan can have mandatory employer and voluntary employee contributions. Both are similar in that all of the employee contributions plus earnings attributed to the employee contributions belong to the employee immediately. Employer matching contributions and earnings attributed to the employer match belong to the employee after a vesting period in a Defined Contribution system. The employee has access to the plan balance subject to a vesting schedule at a termination date.

This is different from another form of pension, the **Defined Benefit** plan, or DB. In a DB plan, the employee gets a benefit on a monthly basis, usually calculated by using a formula of Final Average Compensation (FAC) times a multiplier, times your years of service (YOS). This monthly pension is paid over the life of the employee and may also provide a survivor benefit.

In a DB plan, usually both the employee and the employer make contributions. The plan is invested in the market—generally in stocks and bonds. The employer has a liability for the amount necessary to fund a monthly pension. An important distinction is that the employer takes the market risk. If the market performs better than the expected return of the plan (one of the actuarial assumptions), then the employer's contribution can be reduced, eliminated, or increased. The Michigan Constitution prohibits the decrease of pension benefits in municipal pensions. When a plan's liabilities (the present value of future benefits) exceed the plan's assets, the plan has an Unfunded Accrued Actuarial Liability (UAAL). The employer has to make this up with future contributions.



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In the Deferred Comp and DC pension plans, contributions are fixed and the employee gets the balance when they retire (or when they withdraw it). In a DC or Deferred Comp, there is no possible unfunded liability to the employer, since the employee keeps the plan balance – win, lose or draw. In the DC, the participant assumes the investment risk and receives all of the investment return.

Three Factors of Accumulation

The accumulation in a §457/401(a) plan is based on three factors:

1. **Time** in the plan
2. **Contribution** amount
3. **Rate** of return

All three factors play a role in accumulation, so we shall consider the three independently. All three are highly relevant due to a powerful mathematical calculation called compound interest. The following statement is attributed to the brilliant physicist Albert Einstein: "Compound interest is the most powerful force in the universe." In a DC plan, or in any investment, you start by making contributions, then making interest, then making interest on your interest. At some point, the amount of interest you make can vastly exceed your contributions. By the way, we used the word 'interest' to convey the math principle. In investing, we call it "investment return," which includes interest (which is paid on bonds, money markets or fixed investments), as well as dividends and gains on your investments.

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Factor one: Time is money. Time is a critical factor in any DC calculation (or any investment, for that matter). Here's a chart that shows how much $100 invested per month will accumulate at an assumed 7% annual return over time:

Years	7%
1	$1,239
2	$2,568
3	$3,993
4	$5,521
5	$7,159
10	$17,308
20	$52,093
30	$121,997

With an assumed rate of 7%, saving $100 a month for five years accumulates to $7,159. In five more years, you have now saved $17,308, and have made $5,308 of investment return. Keep going for another ten years and you now have $52,093, which is making $304 a month in investment return—triple your contribution amount! Stay at it for ten more years, and you have $121,997, all for a $36,000 total contribution ($100 a month for 30 years, or if you want to think a little differently, $3.28 a day).

The importance of starting early. Because of the enormous power of compound interest, the sooner you start saving the better off you will be. Take an example of Jack and Jill:

Jill starts saving the day she hires in and contributes $100 a month to her Deferred Comp. She does this for nine years, then stops saving (we don't know why, but she needs to stop for this example). At the end of nine years she has accumulated $14,986. She makes 7% annually on her investments. She doesn't take it out, but leaves it invested and keeps it until she retires 20 years later. When she retires, she has $57,991.

Jack watches Jill save her money and finally decides that he too should begin saving. The year she stops, he starts to contribute to his Deferred Comp. He contributes $100 a month for 21 years and at the end has accumulated $57,098, which is less than Jill's nine years of contributions. Starting early paid off. It's too bad Jill didn't keep it up. If Jill did keep up; she'd have about $122,000. Not bad for only contributing about $3.28 a day.

Factor two: Contributions. As you can see, time is a major factor, as is how much you contribute. It is pretty straightforward: the more you put in, the more you accumulate, proportionately.

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Consider the following chart, which shows different monthly contribution amounts at 7%:

Years	$ 100	$ 200	$ 400	$ 500	$ 1,000
1	$1,239	$2,479	$4,957	$6,196	$12,393
2	$2,568	$5,136	$10,272	$12,841	$25,681
3	$3,993	$7,986	$15,972	$19,965	$39,930
4	$5,521	$11,042	$22,084	$27,605	$55,209
5	$7,159	$14,319	$28,637	$35,796	$71,593
10	$17,308	$34,617	$69,234	$86,542	$173,085
20	$52,093	$104,185	$208,371	$260,463	$520,927
30	$121,997	$243,994	$487,988	$609,986	$1,219,971

As you'd expect, you accumulate twice as much contributing $200 a month compared to $100 a month. Squeeze aside a car payment to yourself ($400), and you could accumulate $487,988 over 30 years. By the way, did we mention that contributions to Deferred Comp are *tax-deferred* and you don't pay current taxes on them? So a $400 monthly contribution will save you federal income taxes (potentially 15% or 25%) and Michigan taxes (4.25%). As a result, your paychecks might only be reduced by about $283 a month.

Graduated Contribution Increases. Many Law Enforcement Officers and Firefighters would like to contribute to Deferred Comp, but can't spare the money for a large contribution at the start of their careers. A solution is to gradually increase the contribution, hopefully as your pay increases. Here's an example:

Rick starts at the department and contributes 4% of his pay. His pay goes up by an average of 2% a year (don't laugh, he might be getting promotions). Every year he adds another 1% to his contribution, until it gets to 10% of his pay; making it painless, and efficient, since he saved money he didn't have (the raise). After 25 years, he'd have accumulated $245,456. If he stuck with his original $120 per month, 4% of his original pay, he'd only have $97,209.

Tax Aspects of Contributions. Another consideration in DC and Deferred Comp is the tax aspect of your contributions. Your paycheck is subject to a variety of reductions, like federal tax, state tax, Social Security (FICA, if you aren't in an exempt system) and Medicare taxes, not to mention union dues and health insurance. In a DC (§401(a)), both the employer and the employee contributions are pre-tax. In a Deferred Comp (§457(b)), you usually make pre-tax contributions, but those have other tax ramifications such as being subject to FICA and Medicare taxes. A new development is the Roth §457, where you may make after-tax contributions that you can later withdraw tax-free. Have a look at the following chart:

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Contributions are subject to:	DC §401(a) employer contribution	DC §401(a) employee contribution	Deferred Comp §457(b) normal	Deferred Comp §457(b) Roth
Federal taxes	no	no	no	yes
Michigan taxes	no	no	no	yes
FICA tax (non-exempt)	no	yes	yes	yes
Medicare tax	no	yes	yes	yes

With DC and 'normal' §457, you are contributing pre-tax dollars. This means that every dollar you are putting in the plan is costing you less than the dollar out of your paycheck. So, you might get $100 in the plan that only takes about $71 out of your check.

The pre-tax savings methods (DC and normal Deferred Comp) use up less of your cash flow since you are contributing both your money and the taxes you would have paid (remember you do pay it back later). The Roth §457 has you saving after-tax money, so you are effectively paying taxes, and saving and growing the remainder tax-free. If you know you are going to be in a high tax bracket later, because you and your spouse have large pensions or other retirement savings, the Roth §457 provides a significant retirement planning opportunity. Roth §457s (and the sister Roth IRAs) allow tax-free accumulation and distribution and are not subject to the Required Minimum Distribution (RMD) rules at age 70½ like DC plans or normal §457 plans. Our basic take on Roth or pre-tax is something like this:

- If you need cash flow now, consider pre-tax;
- If you are in a low bracket now, but will be in a high bracket later, consider Roth;
- If you will have other retirement funds, like spouse's 401(a), IRAs, DROP rollovers, consider Roth;
- If you think you will not need the money later, but want to leave a legacy, consider Roth.

And now factor three, the King: Return. Time is money, and money is money, but return is King. Because of the math of compound interest, return has the greatest effect on accumulation. Return is profound in its change on the overall picture. Have a look at the following chart and watch what happens to $100 a month at various returns:

Years	3%	5%	7%	9%	11%
1	$1,216	$1,227	$1,239	$1,251	$1,262
2	$2,470	$2,519	$2,568	$2,619	$2,671
3	$3,762	$3,875	$3,993	$4,115	$4,242
4	$5,093	$5,301	$5,521	$5,752	$5,996
5	$6,465	$6,801	$7,159	$7,542	$7,952
10	$13,974	$15,528	$17,308	$19,351	$21,700
20	$32,830	$41,103	$52,093	$66,789	$86,564
30	$58,274	$83,226	$121,997	$183,074	$280,452

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Note that a 3% return (maybe all fixed income, for example) would accumulate $58,274, where a balanced portfolio of 7% might generate $121,997, but an aggressive mix of 11% would double the balance to $280,452. We can show you some crazy examples of high returns, but long term, consistent high returns are rare. For example, if we glean the Morningstar® database, only about 13% of the mutual funds in existence today have been in existence before 01/01/96 … 20 years before we wrote this. Only about 852 funds (out of over 30,000) that exist today were around on 01/01/86. Out of the 852 funds, 242 have a return since inception (through 12/31/15) of over 10%. The top-performing fund was Fidelity Magellan (which was rated only one star, or the worst rating, on 12/31/12, and was closed to new investors, so don't get excited). Magellan had a load-adjusted return from its inception in 1963 to 2015 of 16.00%. If you, your dad or your grandpa happened to invest $1,000 in May of 1963, when the fund got started, by 12/31/2015, you'd have about 2.5 million bucks! Of course, if we really want you to weep, we'll talk about buying Apple stock in November of 1983 at around $2.50, or maybe your granddaddy buying you some Berkshire Hathaway with Warren Buffet in 1962 (hint: it was about $11.50, and the stock symbol today is BRK.A). Giant returns are very rare, but fun to look at. Plan for a decent return and be pleasantly surprised when you exceed it.

In the long run, return is a remarkable builder of wealth. For example, consider a Defined Contribution plan where the city contributes 12% and the member (Law Enforcement Officer or Firefighter) contributes 8%. Look at the balances, assuming a 2% annual pay increase, and further assuming the Officer starts at a pay of $36,000:

Years of Service	5%	7%	9%	11%
20	$287,168	$355,272	$442,676	$555,045
25	$429,454	$564,389	$750,516	$1,008,146
30	$548,105	$791,584	$1,154,763	$1,698,785

Note what a small 2% increase can do to the overall accumulation. Also notice how the spread widens the longer the time horizon. Over 30 years, getting 2% more return adds 44-47% to the overall accumulation!

Which leads us to an important observation:

- At the beginning of your savings, how much you **save** matters most;
- When you have a sufficient balance (like $100,000), what you **make** matters most;
- Once you retire, what you **keep** matters most.

Don't mix these up. We see newly minted Law Enforcement Officers and Firefighters wanting to talk about global asset allocation when they have less than $10,000 in the plan. Our advice is to ditch a Starbucks or beer or whatever, and save an extra $100 a month. Conversely, we see guys and gals with $500,000 all in fixed income who want to increase their contributions, when getting an extra 2-3% would be $10,000 to $15,000 a year in the plan in extra returns.

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Here's an example to quantify the idea:

Suppose you look at your spending and find that you tend to buy a couple of cans of pop from the vending machine (at about $1.25 each). You are trying to quit smoking, but you still smoke about a half a pack a day (more on the weekends, less during the week, right?). You'll have a beer or two after work, or more on weekends (don't get us wrong, we like beer), and you stop by the party store and pick up a Powerball or Mega Millions ticket. Let's say you get 5 of those per play. All these things are fun, but can be moderated, if you wanted more money throughout your life (OK, you might win the Mega Millions or Powerball, and that will change your life. If you win, please call us and we will personally help you remain financially independent. If you don't win, you can probably really use our help). How much more? At 7%, here's what those things would add up to in your Deferred Comp plan on a monthly basis:

Years	POP $ 37.50	TIN OF SKOAL $ 120.00	LAST BEER $ 105.00	POWERBALL $ 86.00	ALL $ 348.50
1	$465	$1,487	$1,301	$1,066	$4,319
2	$963	$3,082	$2,697	$2,209	$8,950
3	$1,497	$4,792	$4,193	$3,434	$13,916
4	$2,070	$6,625	$5,797	$4,747	$19,240
5	$2,685	$8,591	$7,517	$6,157	$24,950
10	$6,491	$20,770	$18,174	$14,885	$60,320
20	$19,535	$62,511	$54,697	$44,800	$181,543
30	$45,749	$146,397	$128,097	$104,918	$425,160

Tough choices? Sure. But would you rather have an extra can of pop or $45 grand? One more beer or $128,000? Hundreds of losing lotto tickets or $100,000?

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Differences between Deferred Comp and Defined Contribution Pension. There are specific differences between Deferred Comp and Defined Contribution Pension plans. The primary difference is that contributing to Deferred Comp is strictly voluntary and contributing to a DC is not. The table below summarizes some of the major features of both plans:

Feature	Deferred Comp (§457)	Defined Contribution (§401(a))
Employee contributions	Voluntary	Mandatory
Employer contributions	Usually none	Mandatory
Limit on contributions	$18,500 under age 50 (2018) $24,500 age 50 or over $37,000 make up in 3 years prior to normal retirement age	$18,500 under age 50 (2018) $24,500 age 50 or over Separate from Deferred Comp limits
Withdraw without penalty?	Upon separation from service (any age)	Upon separation from service on or after age 50 (applies to Law Enforcement Officers and Firefighters only). Exception for Substantially equal payments
Loans to participants?	Usually yes (limited)	Usually no (limited)
Vesting?	No vesting requirement, all employee contributions are fully vested	Yes on employer contributions 100% vesting required by normal retirement age or plan termination
Funded in a trust to protect from creditors?	Yes, required	Yes, required
Can be rolled to an IRA?	Yes	Yes
Can be self-directed?	Yes, if plan allows	Yes, if plan allows
Portable?	Yes, can roll to IRA, other §457, or use to buy service credit	Yes, to IRA or other 401(a), 403(b) or §457 (§457: rules apply)
Roth option	Yes, If plan allows	No
Mandatory 70½ distributions?	Yes	Yes

The features are similar, but the common feature of both types of plans is that contributions go into the plan, are invested by you, and accumulate until you use them for retirement. The factors of accumulations for both types of plans are identical:

- How **much** is contributed to the plan;
- How **long** it stays in the plan; and
- How much **return** on investment is made in the plan.

A Note about Bankruptcy Protection. With Detroit's bankruptcy, a significant question is whether DC and/or Deferred Comp plans are subject to the bankruptcy of the municipality. The answer is in two parts: The assets of a §457 or 401(a) plan are in a separate trust and held for the participants. They are protected from the municipality's bankruptcy. The contribution requirement of a municipality to a Defined Contribution plan (the mandatory employer contribution) could conceivably be reduced in a municipal bankruptcy. In the case of a defined benefit plan (like Detroit)

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there may be a future liability for underfunding of the Defined Benefit pension. With a DC plan, there is no underfunding; the municipality is obligated to make a contribution, so the only underfunding would be if the municipality failed to make its contribution, which it is required to do by Michigan law. We won't be surprised to see more municipal bankruptcies after Detroit.

On the flip side, DC and Deferred Comp money *is* protected from creditors of the Officer or Firefighter in a personal bankruptcy or lawsuit. There is an exception in divorce, where a spouse may be entitled to a portion of the pension or Deferred Comp assets pursuant to an EDRO (Eligible Domestic Relations Order). Otherwise pension and Deferred Comp assets are protected from personal bankruptcy. In addition, upon employment separation, if you roll your DC plan to an IRA, the IRA is also protected from personal bankruptcy.

In general, Deferred Comp and DC assets are protected, with exceptions for funding and divorce.

Chapter 1: §457 and 401(a) Checklist

- ❑ Understand advantage of pre-tax savings?
- ❑ Understand effect of time? Estimated balances under certain time scenarios?
- ❑ Understand effect of contribution? Can you find more contributions somewhere?
  - Tax refund?
  - Save part of raises?
  - Cut out some dumb stuff?
    - Budget a daily amount to §457
    - Reduce cost elsewhere?
  - Add 1% a year no matter what?
- ❑ Spouse has high paying job? Consider super saving?
  - You can max both the §457 and the 401(a), allowing more than $37,000 of tax-deferred saving (if under 50) and more than $49,000 of tax-deferred saving (if 50 or over)
  - §457 has special catch up provision to make the super saving even bigger
- ❑ Understand effect of return?
- ❑ Taking steps to have proper mix to increase return?
- ❑ Have annual review of contributions and investment mix?
- ❑ Using §457 to replace Social Security if you are in an exempt system?
  - 6.2%?
  - 12.4%
  - Other?
- ❑ Understand difference between §457 and 401(a)?

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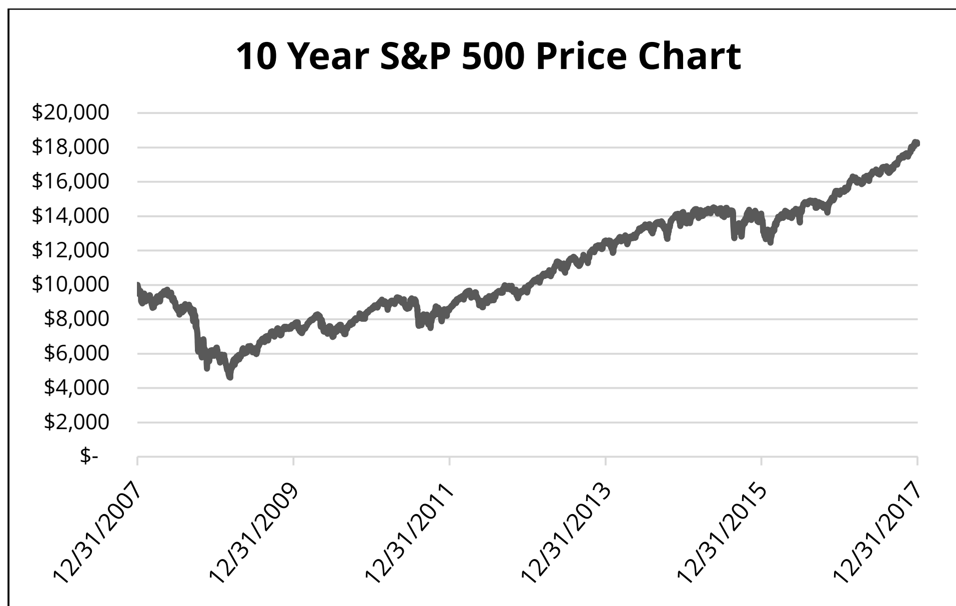
Chapter 2
Maximizing Deferred Comp and Defined Contribution Plans

Now an important question is how to maximize the balances in the plans without prospectively losing money in the long run? With Deferred Comp, contributing more provides more investment and a larger balance. The next question is: How do you achieve a maximum return with minimal relative risk?

Its risk *and* return, not just return. Unless you've been away from civilization for a long time, you know that markets go up and down. Hopefully, you also know equity markets go up in the long run, or at least have so far[1]. As the following chart indicates, the prudent investor who entered the market and stayed in the market, despite all of the ups and downs over the years, realized the largest return! If you are trying to continually hit home runs with investment returns, it leads to the interesting side effect of a record number of strike outs. The key to winning in investing is to not lose. We don't mean lose for a day or for a year. We mean don't miss your goal of having more in retirement. Let's agree that no one has a crystal ball. We don't have one, you don't have one and none of the pundits have one either. And worse than not having a crystal ball is acting as though we do. Therefore, incorporating an insightful investing method that stays in the market would eliminate the need for that mythical crystal ball. First, we need to look at some basics of investments and then we'll get into specifics, including how you may be able to direct investments to achieve an optimal risk-adjusted return.



Source: Bloomberg as of 1/12/2018. For illustrative purposes only and is not intended as investment advice. The charts are shown for illustrative purposes only and do not predict or depict the performance of any investment. Please note: This chart does not include dividends paid. Actual yield would vary if dividends were included.

[1] Past performance is not an indicator of future results.

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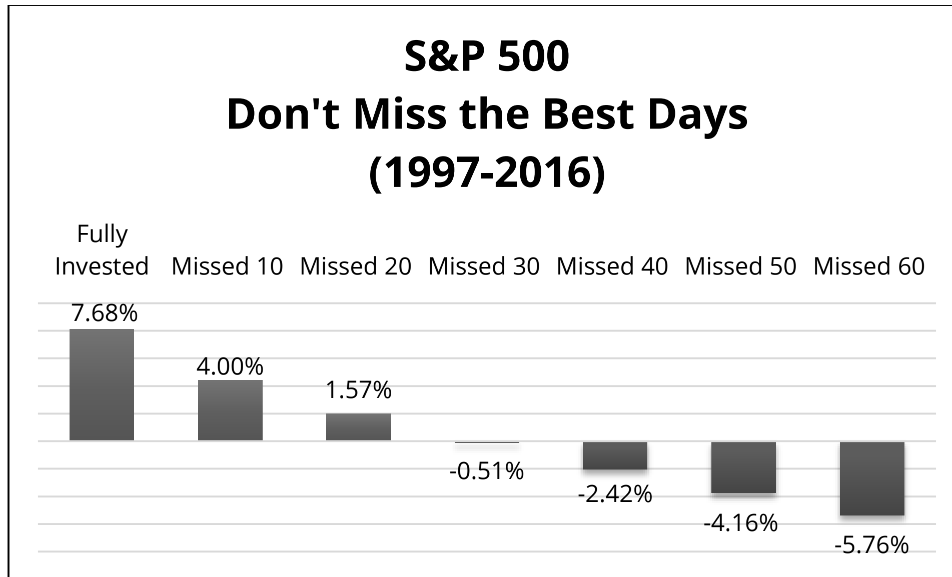

Source: J.P. Morgan Asset Management as of 12/31/2016. For illustrative purposes only and is not intended as investment advice. The charts are hypothetical examples which are shown for illustrative purposes only and do not predict or depict the performance of any investment.

Retirement Investing 101

Investing for retirement has a specific goal: To provide you and your family with a steady stream of cash flow for as long as you live and hopefully have some left over. This is complicated a bit by a tax law that mandates that you start taking distributions from §401(a) DC plans and §457 Deferred Comp plans at age 70½. In general, there are six steps to the retirement investing process:

1. Determine your retirement investment goal
2. Determine your investment philosophy
3. Develop a strategic plan
4. Find the proper ingredients
5. Get invested
6. Review and rebalance

This sounds simple (and it is), but most people put the cart before the horse. Most investors we see are hung up on what fund to buy today, or heard someone talking about gold on CNBC and want to buy gold because the world currencies are collapsing, zombies are attacking or whatever. Retirement investing is like building something: You determine what you want (and can afford), you figure out how it's supposed to serve you, you make a plan, you go to the building supply store and get your stuff, you build it (or hire someone to build it), and you check the finished product. We'd like to point out that having no plan is a plan, just not a good one.

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Your Retirement Investment Goal

Your retirement goal is critical to success. Follow this outline to make sure your investment goal is specific and measurable.

1. Decide what you want:
    a. Here is an example for a DC plan: 'By age 55, I want to have a plan balance large enough to provide me with a retirement income of $50,000 a year, adjusted for 3% inflation, for as long as my spouse and I live.'
    b. For a §457 Deferred Comp plan, it might be different: 'I want the balance in my §457 to be $250,000 by age 53 and I want to maximize that balance in my §457, while protecting the balance from excess risk.'
2. Decide when you want it: Note that in the above examples we set ages.
    a. In DC plans, you really set your retirement age, and the balance can keep growing and accumulating all the while. In the example above ($50,000 a year), it would take about $1,000,000-$1,250,000 in the DC and Deferred Comp plan to accomplish the goal. If, however, our Law Enforcement Officer or Firefighter had only $850,000, he or she could wait, or modify the goal.
3. List the pay-value: This is what you gain from accomplishing the goal.
    a. For the DC: 'If I can accomplish this, I will be able to enjoy my retirement and provide a comfortable existence for my spouse and I, plus leave my spouse and heirs with a sustainable income stream.'
    b. For the §457: 'If I can accomplish this, I can have a great supplement to my retirement and build it through my retirement.'
4. What are the obstacles? These might include:
    a. A bad market can put a big damper on my savings, and a big bear market can reduce my balance below its previous levels.
    b. For a §457, I have to take responsibility for savings, and other 'things' like kids, mortgages, family, and fun can get in the way.
    c. I'm a Law Enforcement Officer or Firefighter, and not an investment expert. I have to have an investment plan, or I might end up selling low and buying high, which will really hurt my balance.
5. What's the plan? You need some form of plan, which might include attempting to save the maximum, and having some investment governance. Your plan may include:
    a. Annually looking at the contribution level, and increasing (and in rare occasions, decreasing) the contributions.
    b. Semiannually (or quarterly) reviewing the investment mix. Is the mix appropriate to the goal? To market conditions? For example, a mix all in fixed income may be temporarily good in a bear (down) market, but is awful in the long term. Conversely, an aggressive (like 80% equities or greater) portfolio is wonderful in a bull (up) market, but painful or even fatal when you start taking distributions (which you have to do at 70½).
    c. Periodically reviewing your investment selection. This is more than just looking at the best performers, it means looking at the managers, the relative performance, and the economic outlook. No single asset class is always the best performer. Sometimes, cash is king. Other times, its domestic stocks or foreign stocks.

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    d. Rebalancing the portfolio to stick to your mix. This is really important because it automates your process. It makes you buy low and sell high, and keeps you from over-investing in risky assets.
6. Ask questions:
    a. Will this work? The short answer is yes. Retirement planning will work. It's a matter of how well it works.
    b. Can I do it? This is a big question. Will you save? Can you take on investment responsibilities? Should you delegate? Is your significant other buying in?
    c. Is it worth it? Heck yeah.

Your Investment Philosophy

You need to think about not just HOW you invest, but WHY you invest. At LJPR, we have a specific creed toward retirement investment philosophy and style. To us, the salient points are as follows, although you may have your own philosophy:

- **Investors are risk averse.** The only acceptable risk is that which is adequately compensated by potential portfolio returns. You reap what you sow. Take risk: make money at the risk of losing some. No risk, less return.
- **Capitalism works.** We believe that capitalism is an effective means of wealth creation, which exists in a free market economy with a functioning legal system. Because capitalism works, we seek to participate in the expansive nature of that system where possible. Most notably, equities offer the potential for higher long-term investment returns when compared to cash or fixed income investments. Equities are also more volatile in their performance. Investors seeking higher rates of return should consider increasing the proportion of equities in their portfolio while accepting greater variation of results (which could include declining portfolio values). Maybe a simple way to look at it is: It's good to have money in the bank; it's better to own the bank. It's good to put gas in your tank; it's better to own part of the oil company that sells you the gasoline.
- **Income is a goal.** We believe portfolios need to provide income, either as retirement income or income for reinvestment and portfolio expansion. Accordingly, we consider income production a significant goal of the portfolio.
- **The World is global.** We see the world as a global economy, with certain effective participants (e.g., US, Canada and Northern Europe), high-growth opportunities (e.g., Emerging Markets such as India or Mexico) and sectors where value appears to have been achieved on unreliable data (e.g., Russia or China). We construct our portfolios based on the parts of the globe that we see as providing a suitable base for honest growth in an expanding system. Investing globally helps to minimize overall portfolio risk due to the imperfect correlation between economies of the world. Investing globally has also historically been shown to enhance portfolio returns, although there is no guarantee that it will do so in the future.
- **Size Matters:** We believe that all big companies were once small, and hence, there are ample rewards to be reaped by having a portion of the portfolio in small capitalization companies (or funds that buy small-caps).
- **Diversification is essential.** We know that diversifying over a wide array of securities and security types reduces risk. Accordingly, we feel that having a diversification of asset classes

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and ingredients in the asset class will reduce the uncertainty of the portfolio as a whole. For a given risk level, an optimal combination of asset classes should maximize returns. Portfolio risk can be decreased by increasing diversification of the portfolio and by lowering the correlation of market behavior among the asset classes selected. Correlation is the statistical term for the extent to which two asset classes move in tandem or opposition to one another. Don't put all your eggs in one basket.

- **Costs matter.** We believe equity returns and fixed-income returns tend to migrate to an average, and that the costs to provide such returns are a direct drag on performance. We will take into consideration the costs of the manager or funds when selecting an ingredient in a portfolio. Furthermore, we feel sales-based fees (like A, B, or C loads on mutual funds) are a further drag, and will try to avoid or minimize any transaction-based costs.
- **Rebalancing reduces risk.** We feel that an effective portfolio is one that has its policies and principles consistently applied. We know that periodic rebalancing to a strategic allocation will reduce the risk in a portfolio, and may enhance return. Since our goal is to reduce uncertainty, we rebalance to reduce risk.
- **Tactics are Sometimes Necessary.** Our general approach is to strategically participate in a global world with both growth and value investment styles, while also generating an income flow. Furthermore, we recognize that markets are a manifestation of human behaviors, and as such, are occasionally impacted irrationally. In situations where the market is particularly irrational, we will adopt a tactical approach, which may include more frequent rebalancing, or shifting between asset classes within Investment Policy Statement guidelines. Tactical shifts in the portfolio will provide for a more conservative investment approach, but should not exceed the client's risk tolerance in terms of a more aggressive approach, unless the client has granted prior approval.

Making the Plan

Ok, you know what you want and you know what you think, so now you meld the two into a plan. The 'Plan' (we're going to capitalize it so it sounds important, because it is) will consist of six ingredients:

1. How much are you going to contribute?
2. Are you using the basic options or going self-directed?
3. What is the appropriate asset allocation or mix of investments?
4. What are the best ingredients (investment choices)?
5. How will you manage those ingredients and mix?
6. How often will you review plan?

If you were a municipal pension system, your Plan would be called an Investment Policy Statement. You'd have a Pension Board and Investment Managers to invest the money. Well, you have, in your §457 Deferred Comp or §401(a) DC plan, a pension system with one person as a participant, **you!** And this personal pension system is very important to provide retirement income to that very important participant.

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Contributions. In a DC pension plan, the city (or municipality) contributes, you contribute and there is no variation. With your §457, you have a choice of how much you put in the plan. So the answer to the question of how much to contribute is 'whatever you determine.' On a Deferred Comp §457, our opinion is to always contribute something, even a tiny amount, and keep increasing it. In the early phases of the Plan, contributions are most important. Focus on saving more and don't worry too much about the investments. You can keep them simple in the early part of the Plan; focus on what goes into the Plan. For Deferred Comp, shoot to get to about 12.4%, and eventually max it if you can. [Note: We once had a Lottery winner as a client who wanted to perpetuate their annual check (this was before the lump sum). They asked us to compute how much they needed to stash from each check to continue the stream. We calculated that if you saved 18.7%, you could closely replicate a stream, depending on inflation and some other factors.]

There is a point we call **'critical mass.'** This is where the annual investment return on your plan balance exceeds the annual contributions. For example, if you are contributing $200 per paycheck ($5,200 a year) and making about 7% on your investments, you reach critical mass at a plan balance of about $75,000. At that point, you are earning as much on investments as you are contributing. Now your money is working as hard as you are. Once you get to critical mass, paying attention to investments will get you the investment bang for your buck we illustrated earlier.

Remember that your contributions are directed by you and your balances are also directed by you. So you need to tell the plan custodian how you want your contributions allocated. This is different than how you want your balances allocated.

Magic Investing: Dollar Cost Averaging. There is a wonderful aspect of DC investing called Dollar Cost Averaging (DCA). It's commonly known that markets go up and down. If you are trying to time your investments to 'buy low and sell high,' you're taking on a daunting task. First of all, it's our experience that deciding when to buy is a different discipline than deciding when to sell. It takes two different mindsets. Similarly, getting out of the market when the market is tanking might sound smart (and temporarily make you feel better), but you now need to get back in.

Enter DCA. DCA is the simple notion that you just keep buying a fixed dollar amount per month (or pay period) irrespective of the markets (you fix market fluctuations with rebalancing). Here's an example: Suppose we have a significant market decline (50%), followed by a recovery to the previous level. Our fund starts the cycle at $10 a share and ends it at $10 a share. During the intervening months, here's what it looks like:

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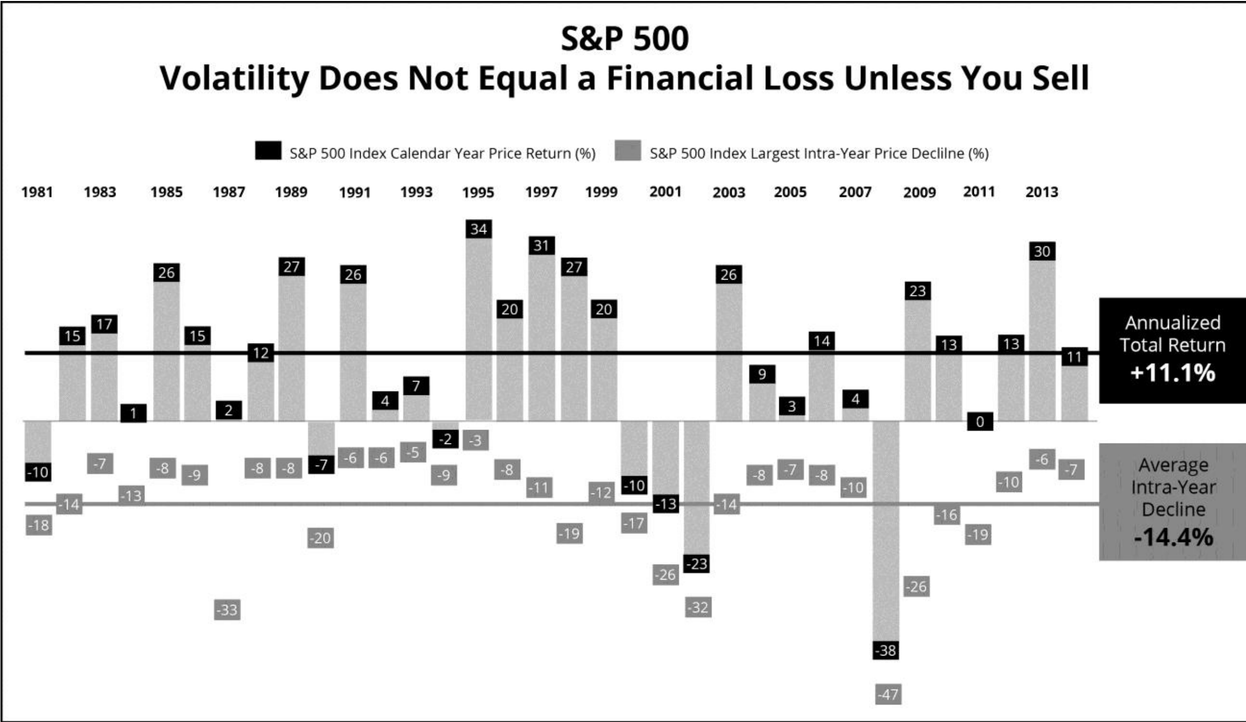
Month	Dollars invested	Price per share	Number of shares	Total shares	Value	Amount Invested
January	$100.00	$10.00	10.00	10.00	$100.00	$100.00
February	$100.00	$9.00	11.11	21.11	$190.00	$200.00
March	$100.00	$8.00	12.50	33.61	$268.89	$300.00
April	$100.00	$7.00	14.29	47.90	$335.28	$400.00
May	$100.00	$6.00	16.67	64.56	$387.38	$500.00
June	$100.00	$5.00	20.00	84.56	$422.82	$600.00
July	$100.00	$5.00	20.00	104.56	$522.82	$700.00
August	$100.00	$6.00	16.67	121.23	$727.38	$800.00
September	$100.00	$7.00	14.29	135.52	$948.61	$900.00
October	$100.00	$8.00	12.50	148.02	$1,184.13	$1,000.00
November	$100.00	$9.00	11.11	159.13	$1,432.14	$1,100.00
December	$100.00	$10.00	10.00	169.13	$1,691.27	$1,200.00

Here's a math quiz: If the fund started the year at $10 a share and ended at $10 a share, the return for the year is 0%. But if you kept buying the fund through the downturn and the upswing, you had $1,691.27 for a $1,200 investment, or about 41%. Note you kept buying. It looked ugly in July, when you had $522.82 in the account and had invested $700.00. At that point you might have wanted to throw in the towel. But the cool thing about DCA is that it keeps you investing.



Source: Bloomberg, 12/31/14. Calendar year returns are price returns, meaning that they do not include the reinvestment of dividends. The index is unmanaged and cannot be purchased directly by investors. Index performance is shown for illustrative purposes only and does not predict or depict the performance of any investment. **Past performance does not guarantee future results**.

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The previous chart shows the volatility of the S&P 500 from 1981 through 2014. During that time the S&P 500 Index has experienced at least a 5% intra-year decline in every year but one. However, equities have still posted positive returns in 26 of those last 34 years with annualized total returns over that period of over 11%.

So let's take a page from Warren Buffet, when asked by a CNBC personality in 2009 how it felt to have "lost" 40% of his lifetime accumulation of capital, he said it felt about the same as it had the previous three times it had happened.

The bottom line is, market corrections do not equal a financial loss…unless you sell.

Real-Life Examples. Here are some real-life examples from Morningstar® using some real funds for the time period of 12/01/07 through 12/31/12, at a $100 per month deposit[2] into each fund:

Fund[3]	Amount In	Value	5 year return static	5 year Return DCA
PIMCO Total Return (A.LW)	6,000	7,309	7.88%	7.82%
Neuberger and Berman Gen I	6,000	7,817	3.67%	10.52%
Fidelity Spartan Index	6,000	7,795	1.61%	10.40%
T. Rowe Price Intl Discovery	6,000	7,873	0.33%	10.80%

There are some surprises: First, we took a bad market period from the beginning of the 2008 market crash. Not surprisingly, all of the three equity funds we picked (Neuberger, Fidelity, and T. Rowe) had relatively low five-year annual returns, from a low of 0.33% to 3.67%. But notice despite the overall five-year return, DCA-ing the equity funds all provided a nice (over 10%) annual rate of return. Note that the fund with the lowest five-year return (T. Rowe Price International Discovery) had the highest DCA return. This is because DCA takes advantage of volatility and price fluctuations. Now look at the bond fund, PIMCO Total Return. PIMCO had a five-year return of 7.88%, pretty respectable, especially compared to the equity funds. But the DCA return is 7.82%, lower than the static return and, lower than the allegedly worse performing equity funds.

Let's suppose you bought the four funds in the above example equally, which would create a 75% equity/25% bond portfolio. If you bought $6,000 worth of each of the four funds on December 1, 2007 and reinvested the dividends and capital gains, by December 31, 2012, you'd have an account balance of $28,494 for your $24,000 investment. Over five years, that comes to an annualized return of 3.49%. If you used DCA, you would have invested the $24,000 at the rate of $400 a month in exactly the same funds, but you'd have $30,793, and an annualized return of 9.9%[4]. DCA lets you buy low and keep buying. It's a great tool and you should use it!

[2] This calculation is from Morningstar® Principia, using a scheduled portfolio function. It assumes no taxes (like a DC plan while funds are in the plan) and reinvestment of dividends and capital gains. Five-year return is annualized total return. Static return is from Morningstar® using five-year return. In every case, the lowest load/fee fund class was selected.
[3] We selected these funds because we see them in §457 plans in Michigan.
[4] From Morningstar® Principia, comparing DCA of $100 a month in each fund starting 01/01/08 and ending 12/31/12 versus $6,000 in each of the four funds starting 01/01/08 and ending 12/31/12. We are assuming reinvestment of dividends and capital gains, and no taxes.

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Basic or self-directed? Providers of DC type plans (ICMA, Nationwide, Fidelity, Prudential, etc.) have a set of choices you can make in your investments. The basic plan inevitably includes target plans and specific funds. Some plans (you have to check with your municipality's HR department) allow you to go outside the basic options and buy pretty much anything. This can be thousands of choices of mutual funds or even individual stocks. More choices mean the possibility of better ingredients and better mix, but also more work and more opportunity to pick duds or do stupid stuff. For example, with a self-directed option, you can focus on certain parts of the world, or certain industries, or certain asset classes. You can refine your mix to include the whole spectrum of investments. But, 'whole spectrum' includes the bad performing funds, or expensive options, or crummy stock tips from friends or relatives.

Target Funds: Plug and Play. All the DC plans and §457 plans we work with have some form of a target fund. A target fund usually has a 'target date' of when you intend to retire. These funds usually say 'Target 2020' or 'Target 2050.' The target funds are great when you are starting out. In fact, we suggest those strongly for new members: focus on saving money and don't worry about investing for a while (until critical mass, for example). Target funds are simple and do follow one very important rule: they diversify your investments. Some things you should know about targets:

- The farther the target date from the present time period, the more equities therefore risk (and ideally return). A Target 2050 will have more stocks than a Target 2020.
- The funds rebalance, but not often. Rebalancing means to reset the mix to the correct recipe. Rebalancing is not as important when you have a small plan balance (which is why we like targets for starting out), but is very important for reducing risk later when you have a significant plan balance.
- The plan custodians tend to load their own funds into the target allocations. This means you may be getting under-performing funds in your target fund. Look into the funds used in the targets.
- You can customize your target plan by buying more than one. For example, if you want a Target 2025, you can blend a 2020 and a 2030 target.
- All target funds are not created equal. In a recent study by Morningstar®, Target 2015 funds by different providers had returns ranging from positive 2% to negative 4% for the same target date.
- Fees matter. In the same study by Morningstar®, the fees for target funds ranged from 0.18% to 1.31%. As we pointed out earlier, the fees come out of your pocket, so the higher the fees the lower your relative performance.[5]

We find that target funds are good for members who want a 'plug and play' option that is simple. The targets don't necessarily optimize performance, but provide an easy starting point. From there, you can build a retirement portfolio within the funds or self-directed option.

[5] Target-Date Series Research Paper. 2013. Morningstar.

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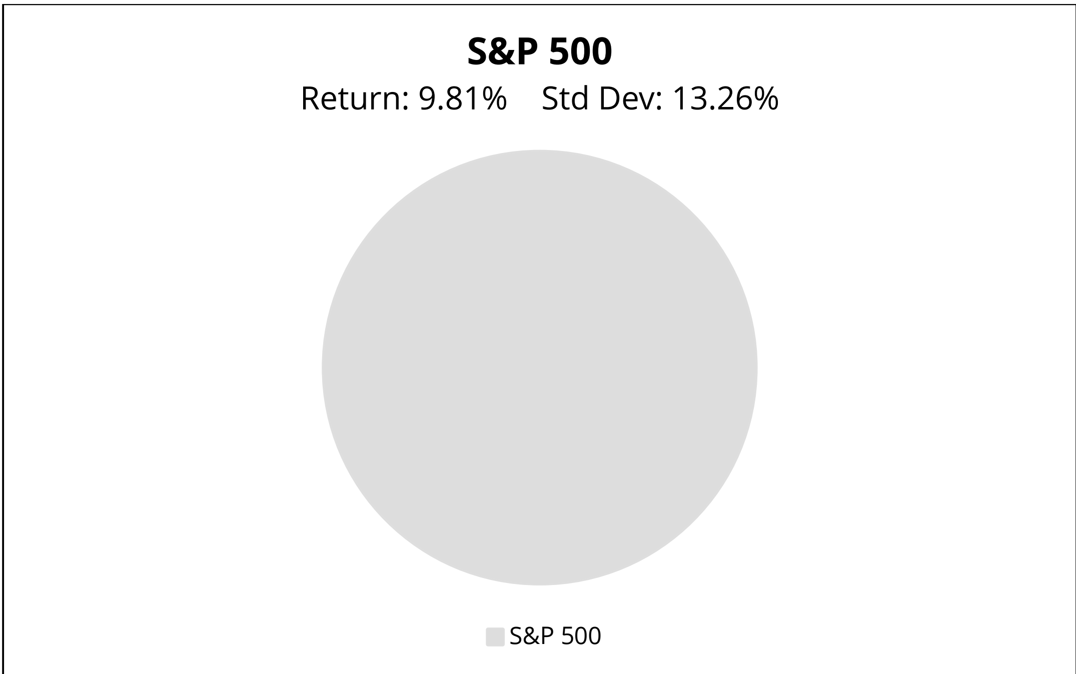
Investing on Your Own: Making a Mix – Asset Allocation

Now we can get to the basic concept of investing retirement money: creating a mix. The concept of asset allocation is to get the right mix (for you) of low-volatility stuff (like fixed income) and stuff that grows (like equities). Think of it like a car: how big of an engine do you want (equities) versus how much safety equipment (fixed income/bonds). For the most part, all pension systems invest their money this way, in a mix of equities and fixed income. No large pension system we can find will try to 'time the market' by getting in or out at some specific time. For one thing, it's too darn hard, and for another, you never know the unknown factor, like 9/11, that can bite you. Big pensions have a legal obligation: to provide the most retirement income with the least amount of relevant risk. We think this is a good goal for both big retirement plans and retirement plans with one participant.

How asset allocation works:



Consider the return and risk on a plan that has all its money in the stock market—in this case—the S&P 500. The return from January 2002 to December 2017 is about 9.81% a year (not bad). The risk, as measured by standard deviation (Std Dev), is 13.26%, which is a lot of up and down risk. Our goal, through asset allocation, is to reduce risk, and hopefully increase return. Remember that risk is very ugly in the actual distribution phase of retirement.

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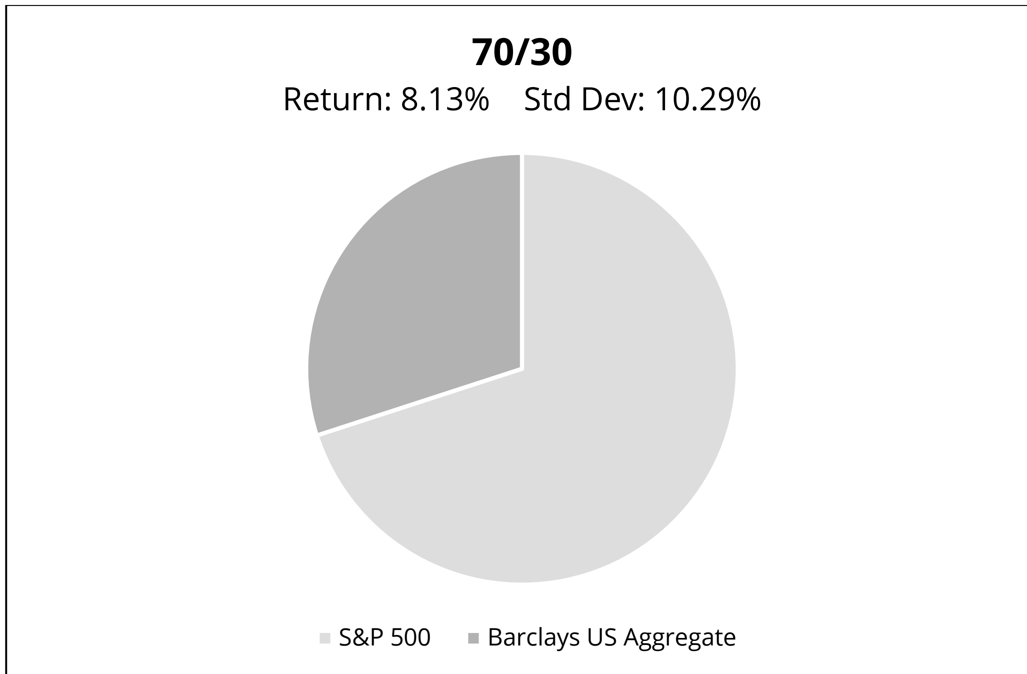
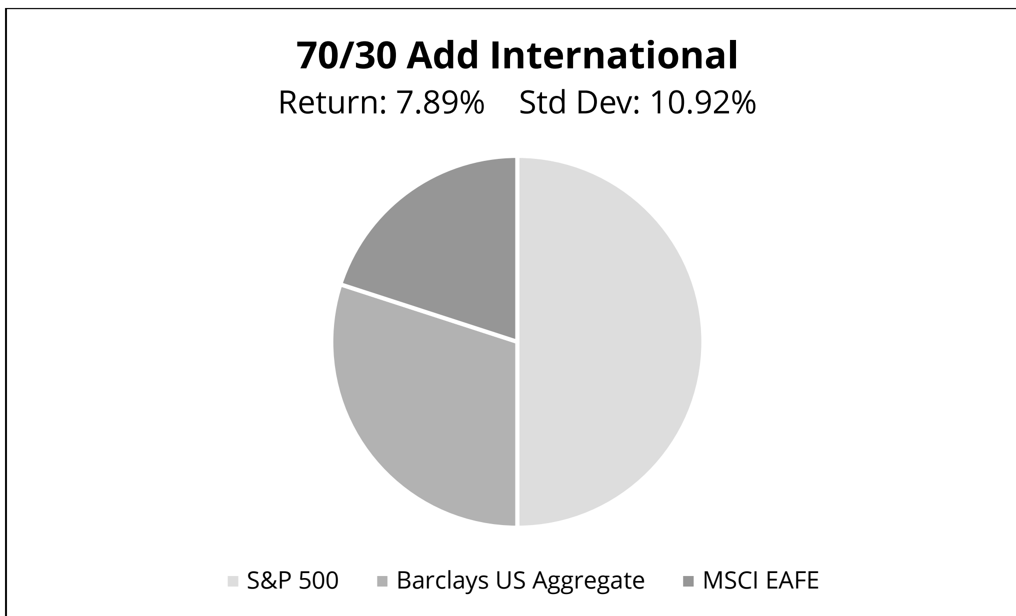


We add some bonds, or “airbags,” to protect us in the event of a crash. We’re adding 30% into the bond side. The return went down, but not too much, and the risk went down quite a bit. We lost about 1.68% return to cut risk by 2.97%. Seems like a good trade-off (it is).



We think the U.S. is the greatest country in the world (can’t say the same about our politicians), but the world as a whole has more growth potential, and more diversification than just the US markets. We add some international stuff, and the return goes down and the risk stays relatively stable. Now we have 7.89% return and 10.92% risk. Let’s see if we can do better.

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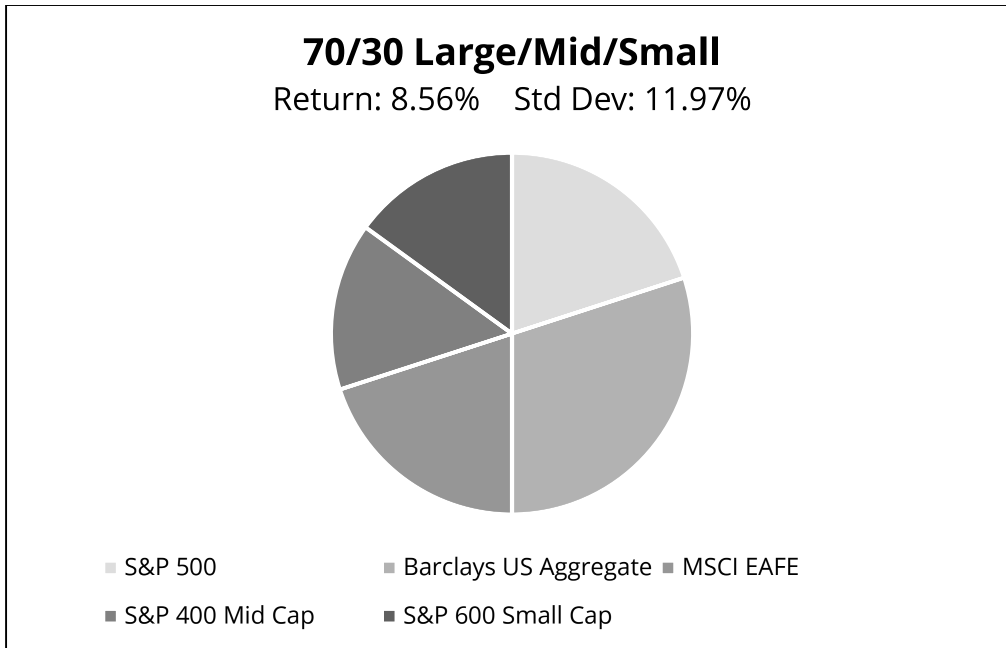
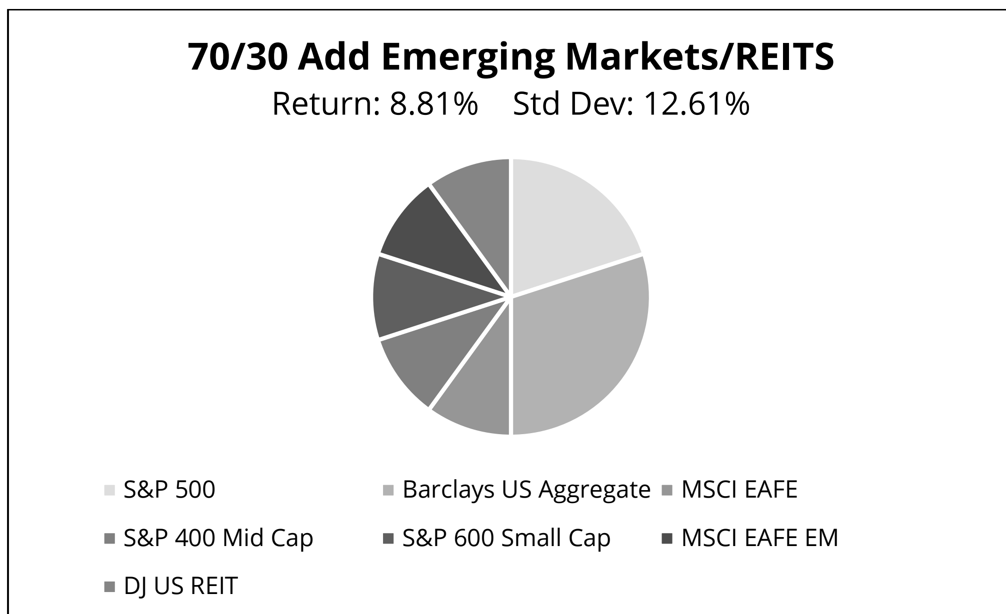


We challenge you to name a big stock that wasn't once a small stock. Think of any? Small-caps might turn into mid-caps, which, again, might turn into large-caps. When Apple was a tiny company, the growth rate was much greater than when it is worth over $400 billion. If we add small and mid-cap U.S. stocks, which tend to grow faster and be riskier, we see a logical outcome: Return is up and risk is up. Let's go further. Return now up to 8.56% and risk slightly up to 11.97%.



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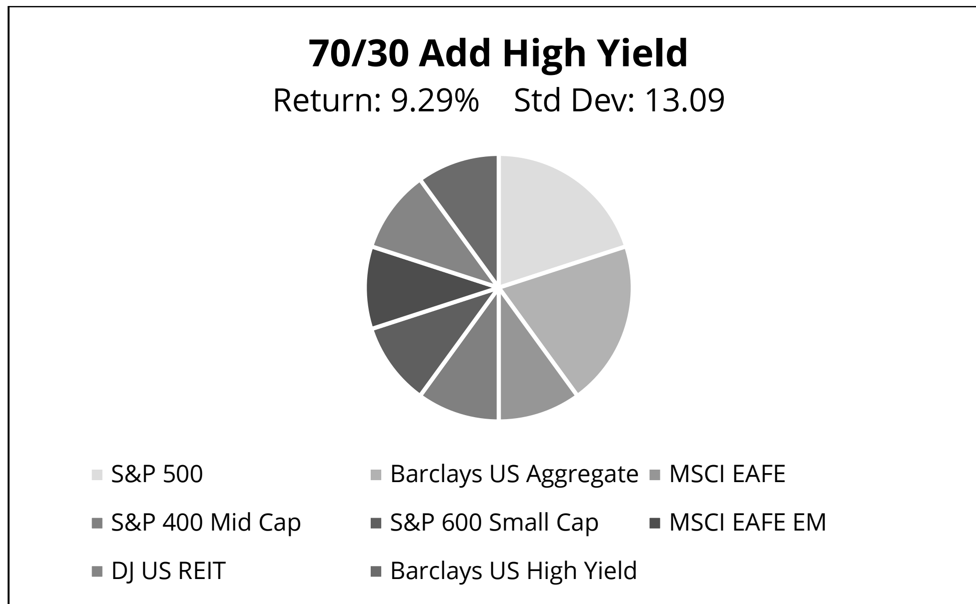
There are about 900 million people in North America, Europe and Japan. There are about 3.5 billion in the growing emerging markets. Now, more than half the world's growth is in emerging markets, such as China, Brazil, and Mexico. These markets have risk, but a lot of return and a lot of room to grow. We add something risky and what happens? The return goes up to 8.81 % but the risk goes up to 12.61%. Can we do one better?



Now we add high-yield bonds (also called junk bonds) to the pile. We have gone almost full circle: we have the long-term return very close to the stock market with lower risk. It's the miracle of asset allocation.

Rebalancing

Rebalancing is a technique that is used to reduce risk. It is a well-proven axiom of investing that the mix (as we saw above) is extremely important. Different asset classes produce different returns over time. In general, the riskiest asset classes tend to produce higher returns. If you started out with the 70/30 mix we used as an illustration, that mix would morph into a riskier and riskier portfolio over time, all while you got closer and closer to needing the money (at retirement). To stop this upward risk spiral, we use a technique called rebalancing, or periodically resetting the portfolio back to its original mix. This does a few things:

- Provides opportunity in down markets by re-allocating to equity investments. 'Buy low.'
- Reduces risk in up markets by re-allocating to the safer fixed investments. 'Sell high.'
- By automating the process, rebalancing helps prevent making a timing decision.

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Don't get all excited about rebalancing being a 'timing' mechanism. It isn't. Rebalancing has a main purpose of reducing risk. It can increase return in volatile markets, but the long-term direction of markets is up. We could give you a bunch of examples, but a good one is from a study by Vanguard[6].

Comparison of 60% stock / 40%[7] bond portfolios 1926-2009:

1926 through 2009	Monthly Rebalance	Never Rebalance
Maximum stock %	68	99
Minimum stock %	52	36
Final stock %	61	98
Average annual return %	8.5	9.1
Annualized std. deviation (risk) %	12.1	14.4

This study is pretty interesting. It takes a long time period (1926-2009) which covers the best of times and the worst of times. Note that if you didn't rebalance, you ended up with 98% stocks. If you were investing retirement funds, do you think 98% stocks is a good idea for sleeping at night? What is more telling is that rebalancing to stay around 60% stocks reduced annualized return from 9.1% to 8.5%. However, volatility (risk) went down from 14.4% to 12.1%. That's a 19% reduction in risk for a 7% reduction in return.

How often should you rebalance? This is a great question and the answer is surprising. The same Vanguard study took that same time period (1926-2009) and compared rebalancing a 60/40 portfolio monthly, quarterly, annually and never. Since rebalancing makes sense, you'd tend to think more frequent was better, but look at the statistics:

Frequency	Monthly	Quarterly	Annually	Never
Average equity %	60.1	60.2	60.5	84.1
Annual turnover %	2.7	2.2	1.7	0
Number of rebalances	1,008	335	83	0
Average return %	8.5	8.6	8.6	9.1
Volatility %	12.1	12.2	11.9	14.4

It's evident that rebalancing reduces risk. The possible surprise is that rebalancing works better if you don't do it too often. Annual rebalancing actually makes more and is less risky in this time frame than monthly rebalancing. We suggest that our clients rebalance on their half-birthday (the date 6 months from your real birthday). You'll have something on your calendar and it won't interfere with your real birthday.

[6] "Best Practices for Portfolio Rebalancing" July 2010, Jaconetti, Kinniry, and Ziberling. Vanguard Research.

[7] S&P 500, Barclay's Aggregate Bond Index.

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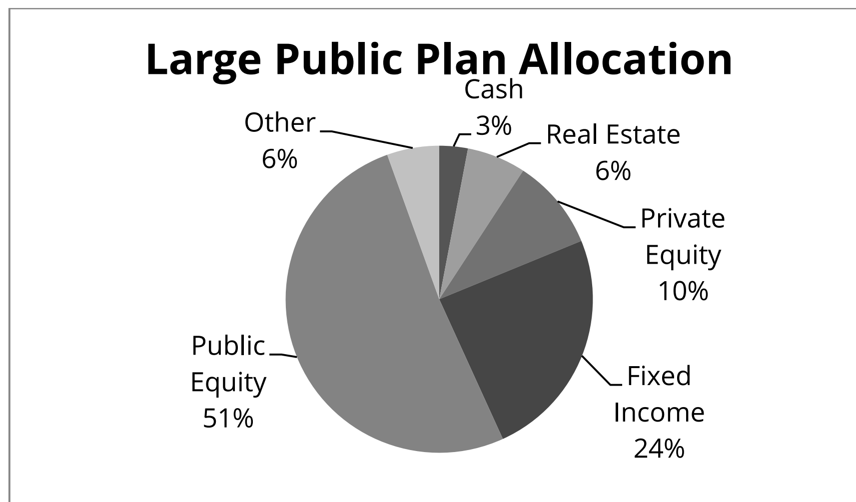
Rebalancing with income. Another way to rebalance, which works very well, is to use your contributions to rebalance. Instead of resetting the allocation of your balances, you direct your contributions to the disproportionately low asset class. If the market was down, you'd direct your monthly contribution to equities (that old 'buy low' again) and if the market was high, you'd direct your contributions towards bonds. Here's a chart from the Vanguard study, which again highlights the effects of directing income and dividends to rebalance:

Frequency	Monthly	Income	Never
Average equity %	60.1	61	84.1
Annual turnover %	2.7	0	0
Number of rebalances	1,008	0	0
Average return %	8.5	8.5	9.1
Volatility %	12.1	11.3	14.4

The bottom line is that rebalancing is a great technique for reducing risk in your retirement portfolios. We use it in our practice and in our own portfolios.

Some Logical Mixes: When trying to determine the right mix for your retirement portfolio, there are some useful guidelines. In general, we look to big pension plans to determine what allocation they use to achieve their goal. This echoes something we said earlier: your DC plans (that includes your §457 and maybe your DC) are retirement money, and should be invested as such. The aggregate of large public pension plans[8] hold assets in these categories:



[8]Private Equity Growth Capital Council, Public Pension Fund Analysis report 09/12. 151 large public funds were analyzed, each with over $1 billion.

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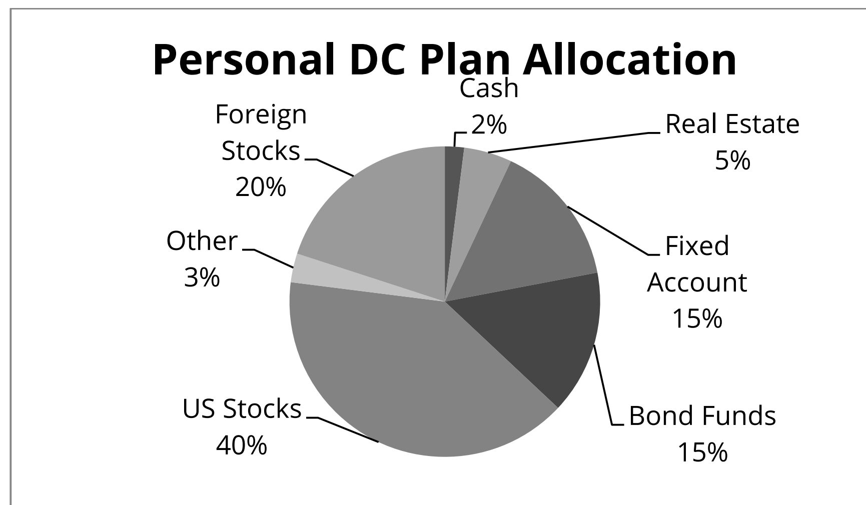
You can see that the big plans allocate a majority of their assets (about 70%) to the riskier side, like equity (stocks), real estate and private equity. Private equity is a special form of alternative investment where the investor buys privately held businesses (like when you hear about a private equity fund buying a company). For a normal self-directed DC or §457 plan, a parallel portfolio might look like this:



You can modify the allocation to your personal situation. Here are some factors to consider:

1. What is your general nature (stocks/fixed income)?
   a. Conservative (50/50)
   b. Moderate (60/40)
   c. Moderate aggressive (70/30)
   d. Aggressive (80/20)
   e. Very aggressive (100/0)
2. Answer the same question about your spouse.
3. How close are you to retirement? The closer you are to retirement, the lower the risk, and lower the percentage of equity.
4. How long before you will take distributions? Remember that §457s and DC plans require distributions at age 70½[9]. In general, we tend to stay more moderate or aggressive for a long horizon to distributions and more conservative for a short distribution horizon. The reason is simple: DCA works great in a moderate or aggressive portfolio because the volatility allows you to increase holding at low points. If you are taking withdrawals in a volatile portfolio, you can be taking out in a down market, which can be painful or financially fatal.
5. What other sources of income do you have?
   a. Defined Benefit plan
   b. Social Security
   c. Retirement job
   d. Spousal income

[9] This is true of §457 plans, DC plans, and regular (and rollover) IRAs. The rule is called the Required Minimum Distribution (RMD) rule. Roth IRAs are not subject to RMDs.

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Finding Great Ingredients

Investing for retirement is like preparing a meal. You need a great recipe (asset allocation) and great ingredients (mutual funds or other investments). The asset allocation can impact how well your portfolio will perform in the long run. Stock picking and timing is only a fraction of determining return. However, you still have to pick what mutual funds you want to invest in. Your retirement plan will give you a "menu" of mutual funds and investments to choose from. So, what should you look for in a fund? Generally, there are five main ingredients that make for a good fund:

- Return (relative to other similar funds)
- Risk (relative to other similar funds)
- Fees. Fees matter… a lot. The fees reduce the return and you pay the fees.
- Manager and track record
- Size of the fund

The obvious first thing to look at is return. How well is the fund doing compared to similar funds in the same category? Make sure you are doing an apples-to-apples comparison. For example, the S&P 500 index fund, which is 100% stocks, is not going to be a good comparison to a balanced fund (stocks and bonds) or to a bond fund.

Also, pay attention to the risk-adjusted return, which is how much risk you are taking to achieve that return. Measurements like standard deviation are prime examples. Morningstar® is one source to provide these numbers. You can have two funds with the same performance, but a much different risk level. Pick the fund with the lower risk score.

Another consideration is fees. Is there an up-front commission (A-shares)? Is there a back-end load commission (B-shares)? Is it a no-load fund? What are the 'unseen' fees, such as the annual operating expense or 12b-1 fees? The greater the fees, the less money you have working for you. Fortunately, most DC plans use no-load funds, which have only a management fee. However, when comparing two very similar funds, the fees matter in the selection. In other words, if everything is equal, go to the less expensive fund.

A fourth thing to consider is how long the manager or investment team has been with the fund. If a fund has a great 10-20 year track record, but the current manager has only been with the fund a short time, then they weren't responsible for that performance, and since there is no history with this manager there is an unknown. This is not necessarily a deal breaker, but something to look for, especially if it can be a tiebreaker. That being said, keep in mind that not every fund is going to excel at all of these characteristics. However, using these guidelines can help you narrow your choices.

Lastly, consider the size of the fund. Sometimes size matters in funds, but not the same way it does in stocks. For mutual funds, smaller can sometimes be better. When we say smaller, we mean the assets that are in the fund. Some funds can be in the billions. Some funds like the Vanguard Total Stock Market index have over $380 billion. Why can smaller be better? Take a small cap fund, for example. This type of fund invests in smaller companies that tend to have less stock out in the market to buy. Let's say the fund is doing really well and more and more people start to invest in it. This large inflow of cash can create a problem in that it "forces" the manager to invest the money in a timely basis in order to put it to work. He has more money than product and can be pressured into picking something, anything, which isn't always ideal for the mutual fund. This can go against the

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fund strategy. Have you ever noticed that some popular funds have closed to new investors? Sometimes it has become too large so they close it to remain nimble and not deviate from their strategy. Conversely, for bond funds and index funds, this is not an issue. Actually, it is just the opposite. These types of funds are easy to manage and the larger asset base allows expenses to go down as they are more spread out. So, bigger is better in this case. Confusing, we know.

When is a fund too large? Great question. Basically, it comes down to performance. If a mutual fund cannot maintain its historical performance in relation to its peers or maintain its strategy, due to its burgeoning size, then it is an issue. Note that just because a fund is huge, doesn't mean it isn't effective. It is when that size hurts performance or "forces" the manager to deviate from the funds strategy or take on unnecessary risk. There are always exceptions. Not all large funds are bad.

A lot to remember, we know. With all these factors in mind, remember that allocation is the key. A little bit of everything goes a long way and reduces volatility.

Chapter 2: Investing Checklist

- ❑ Understand why to stay invested?
- ❑ Set a retirement investment goal?
- ❑ Determine your investment philosophy?
- ❑ Create an investment plan?
  - Contributor level (§457, 401(a), DROP, Roth, etc.)
  - Options within the investments?
  - Asset allocation?
  - Best funds or ingredients?
  - How will you manage?
  - How often to review?
- ❑ Understand dollar cost averaging?
- ❑ See how mix reduces risk?
- ❑ Understand rebalancing?

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Chapter 3
Withdrawals from Defined Contribution or Deferred Comp

Say you have been following good advice (hopefully ours) and stashing a regular contribution and investing it wisely. You decided to retire. Now what? First, you have to understand that DC (§401(a)) and Deferred Comp (§457) are two different animals in respect to how withdrawals are taxed. In general, you can take a Deferred Comp withdrawal at any time after you separate from service (quit or retire) without a penalty. You pay taxes on the distribution, but no penalty.

DC plans and §457 plans are taxed differently:

Feature	§401(a) DC Plans	§457(b) Deferred Comp Plans
Taxation	Fully taxable as withdrawn	Fully taxable as withdrawn
Early Withdrawal Penalty (before age 59 ½)	Yes, 10% if withdrawn before age 59½ (50 in some cases for Law Enforcement Officers and Firefighters if you stay in the §401(a)).	No penalty on §457 accumulations. 10% on amount rolled from §401(a) and 401(a)
§72(t) (SEPP) to avoid 10%	Yes, pre 59 ½ with restrictions (minimum 5 years or age 59 ½)	Unnecessary
Rollover to IRA or other plan?	Yes to IRA, §457(b) (public), 403(b) and 401(a)	Yes to IRA, §457(b) (public), 403(b) and 401(a)
Minimum distribution at 70 ½?	Yes, age 70½ or retirement, if later	Yes, age 70½ or retirement, if later

For tax reasons, we usually advise keeping the §457 and §401(a) separate, especially if the Law Enforcement Officer or Firefighter is under age 59½. Note that the DC plan is more restrictive than the Deferred Comp in its tax treatment. Many times, we will look at the age of the retiree, and use the Deferred Comp as the flexible pre-59½ distribution. For example, if we get a 57 year old with a $650,000 DC balance and a $200,000 Deferred Comp balance who needs $30,000 a year, we'll segregate at least $80-$90,000 in the fixed portion of the Deferred Comp to use until they reach age 59½[10]. That way, we have a few years covered. We'll roll the DC over into an IRA for more investment options and then reconsider the strategy at age 59½ and at age 62, when they probably will start to receive Social Security (if they are eligible).

[10] We like to build an 'emergency cushion' that is bigger than is needed (like 120-150%).

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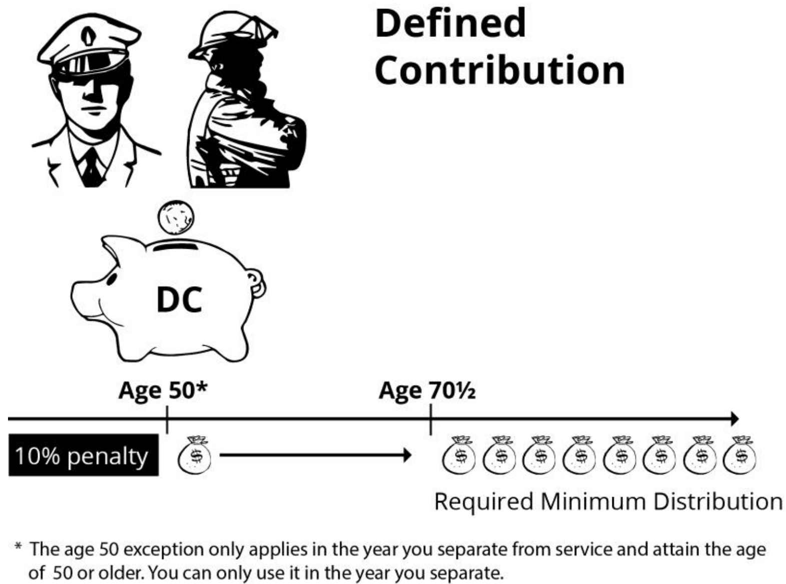
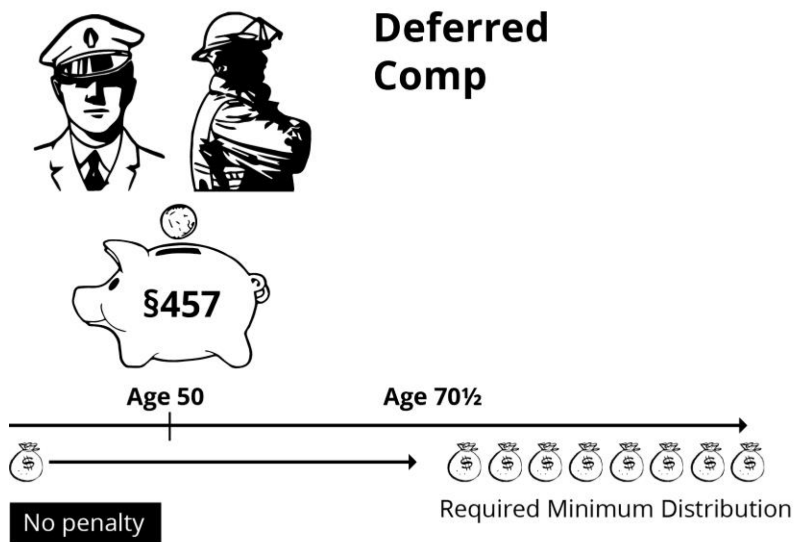
Here is how the DC taxation looks:



Money in a DC plan is subject to a 10% penalty if a Law Enforcement Officer or Firefighter takes the money out before age 50 and separation from service. At age 59½, they can roll the DC into an IRA, and take distributions from the IRA. At 70½, they must begin taking distributions or suffer a 50% (yes 50%) penalty on the Required Minimum Distribution.

Deferred Comp is easier:



There is no penalty on Deferred Comp if you leave service, so you have the flexibility to take it at any age.

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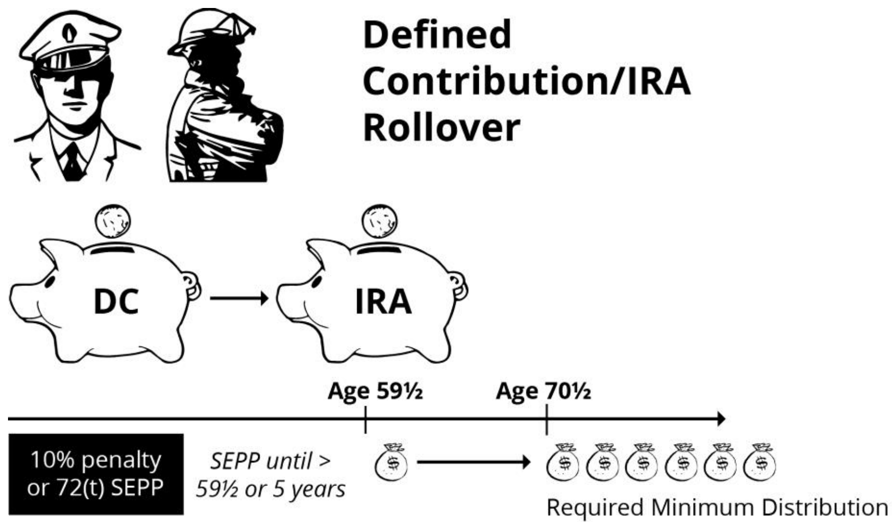
You can roll the DC (and Deferred Comp) into an IRA. Here you change the characteristics of the assets. You lose the age 50 exception and you lose the no-penalty exception. If you are already 59½ when you retire, the rollover is usually the best option. If you are close to 59½, then using the Deferred Comp and rolling over the DC might make sense. If you are getting another job and will be OK with funds, the IRA rollover makes sense. If you are age 52 or 53, actually retiring and using the DC for funds, you may consider leaving the money in the DC plan until you reach age 59½.



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How Much to Withdraw?

A major issue in DC and Deferred Comp plans, as well as IRAs, is 'how much can I safely withdraw?' This question is a good one, and has a simple answer and a complex one. The simple answer is that if you balance your investments in a good retirement mix and rebalance to reduce risk, you can withdraw up to 4% per year and maintain your starting balance and generally keep some of your purchasing power (inflation-adjusted). Simply stated, if you are making 7%, and taking out 4%, you are growing the balance (and your withdrawals) by 3%. If only it were that easy. Market returns aren't in a straight line, but go up and down. For example, here are the returns of the years 1989-2008, in the order they happened, and in the inverted order:

Year	1989-2008	2008-1989
1	31.69	-37
2	-3.11	5.49
3	30.47	15.84
4	7.62	4.91
5	10.08	10.88
6	1.32	28.68
7	37.58	-22.1
8	22.96	-11.88
9	33.36	-9.11
10	28.58	21.04
11	21.04	28.58
12	-9.11	33.36
13	-11.88	22.96
14	-22.1	37.58
15	28.68	1.32
16	10.88	10.08
17	4.91	7.62
18	15.84	30.47
19	5.49	-3.11
20	-37	31.69
Average	**8.43%**	**8.43%**

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So far, so good. Here is a question: if you made an average of 8.43% a year over 20 years, you should be able to take out 5% and increase that by 3% a year, you would still have all your money plus some, right? In fact, if you are math-inclined (we are), you'd figure out that you should have, in a straight line 8.43% portfolio, about twice as much as you started with. So if you had $1 million in your DC and Deferred Comp and you started taking out $50,000 a year and gave yourself a 3% raise each year, by the end of 2008, you would have about $2.06 million. But reality is stranger than the projection. If you actually took the $50,000 plus 3% a year from 1989-2008, you'd still take the same amount and your balance at 2008 would be about $3.075 million! Now here's the startling reality that shows the opposite of Dollar Cost Averaging. If you took the same out and inverted the return (remember it's 8.43% either way), you would only have about $164,000 left! Look at the numbers:

8.43% Actual Return	Actual 1989-2008	2008-1989 Inverted
$2,062,716	$3,075,123	$163,636

More on Taxes:
Tax Brackets: It's important to understand how tax brackets work. Michigan Law Enforcement Officers and Firefighters have some specific tax characteristics.

Federal Tax:

- Standard Deduction or Itemized Deductions, whichever is greater;
- Brackets starting at 10% and rising to the top bracket of 37% for 2018 and beyond;
- Special rules for Law Enforcement Officers and Firefighters taking distributions at age 50 or later.

State of Michigan Tax:

- Exemptions for the taxpayers and dependents;
- DC distributions may be subject to Michigan Income Tax ;
    - For **retirees born before 1946**, there will be no changes to the taxation of Social Security, public and private pensions or interest and dividends. The maximum allowable pension deduction for single individuals on returns filed for tax year 2017 is $50,509 and $101,019 for married individuals.
    - For **retirees born between 1946 and 1952** there will be changes depending on when you turn 67. Before age 67, there will be a limited subtraction ($20,000/$40,000) for private and public pensions and the subtraction for dividends and interest has been eliminated. Once you turn 67, the limited pension subtraction will be replaced by a limited subtraction (again $20,000/$40,000) against **all income** regardless of source. Social Security continues to be exempt both before and after age 67.
    - For **retirees born after 1952**, there will be changes depending on when you turn 67. There is no pension subtraction before age 67 (either public or private). Social Security is still exempt and there is no interest/dividend subtraction. Once you turn 67, you can elect an exemption ($20,000/$40,000) against all sources of income and personal exemptions are not allowed. Alternatively, you can elect to exempt Social Security, certain pensions and claim personal exemptions.

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SSA exempt employment is not covered by the federal SSA, which means the worker did not pay Social Security taxes and is not eligible for Social Security benefits based on that employment. Almost all employment is covered by the federal SSA. The most common instances of pension and retirement benefits from employment that is not covered by Social Security are law enforcement and firefighter retirees, some federal retirees covered under the Civil Service Retirement System and hired prior to 1984, and a small number of other state and local government retirees. Federal retirees hired since 1984 and those covered by the Federal Employees' Retirement System are covered under the SSA.

Recipients born between January 1, 1946 and December 31, 1952 who receive pension or retirement benefits from employment with a governmental agency that was not covered by the federal SSA are entitled to a greater retirement/pension deduction or Michigan Standard Deduction. If you or your spouse are SSA exempt, this increases your maximum allowable deduction by $15,000.

Big distribution tax effects. Because DC distributions can be flexible, you can take more than 3% or 4% of the balance. Taking a big distribution in a year can not only incur tax on the distributions but also shift a Law Enforcement Officer or Firefighter into a higher tax bracket. Because of other tax rules, distributions can cause a variety of other tax costs:

- For 2018-2019, medical deductions are subject to a 'floor' based on Adjusted Gross Income (AGI).
- College tuition deductions are above the line, but also subject to income limits.
- Certain credits, particularly education credits, like the HOPE and Lifetime learning credit, are subject to limits on income. Extra income from a DC can eliminate these credits.
- At higher income levels, itemized deductions, like mortgage interest, property taxes and charitable donations, are reduced.
- At higher income levels, personal exemptions are phased-out.
- If you take a really big distribution, you can climb into the top brackets and your capital gain and dividend tax rates rise by 33% and you are subject to an additional 3.8% tax on dividends, interest and capital gains (over $250,000 AGI for married and $200,000 for single).
- If one spouse is collecting Social Security, the increase in income can make more of the Social Security taxable.
- If you are enrolled in Medicare, higher income can generate higher Medicare B premiums.
- You can run over the exemptions (if any) for pensions in the state of Michigan and pay Michigan tax on more of the distributions (see maximum deductions based on age above).

50 and over rule for 401(a). Another important rule in looking at DC taxes is the special rule for Law Enforcement Officers and Firefighters. DC plans allow a penalty-free distribution after age 50 (as long as you are separated from service in that year).

For all types of plans, distributions are taxed upon withdrawal. If the person is under age 59½, they may have to pay a 10% penalty for an early distribution. Exceptions to this penalty include:

- Distributions on account of the death of the participant;
- Distributions on account of disability of the participant;
- Distributions to a public safety Officer (e.g. Law Enforcement Officer or Firefighter) age 50 or older;

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- Distribution of substantially equal period payments (this is called the §72(t) exemption);
- Distributions directly rolled into or transferred into an IRA.

For most Law Enforcement Officers or Firefighters near 59½ or working at another job, making a transfer from a DC to an IRA is the most flexible option. The IRA allows the Law Enforcement Officer or Firefighter to select distributions within certain guidelines and has an almost infinite range of investments.

With a DC transfer, the recipient IRA is called a Rollover IRA. For rollover IRAs, distribution options include the following:

- **Pre-age 59½ distributions.** Distributions prior to age 59½ are subject to a 10% penalty unless exemptions are met. The only salient exemption to the penalty is the 72(t) exemption for substantially equal payments. **The age 50 exemption does not apply once a DC is transferred to an IRA**.
- **59½ - 70½.** Between the ages of 59½ and 70½, a participant can take any distribution they choose. All distributions are taxable.
- **Age 70½.** At age 70½, a participant must start taking distributions or face a 50% (not a typo) penalty. The Required Minimum Distribution (RMD) is based off an IRS chart called 'Table V,' and is calculated by taking the end of year balance from the prior year (12/31) and dividing by the life-expectancy from the table. Obviously, the older you get, the shorter your life expectancy, and thus the higher percentage you must withdraw.
- **Roth Conversion.** You can convert a tax-deferred traditional IRA into a tax-free Roth IRA. Roth IRAs are tax-free in growth and income, and upon distribution. Roths also are not subject to the Required Minimum Distribution rules, so a Roth can be passed to a spouse or children (or grandchildren, for that matter) tax-free. The rules on Roth conversions are complex and beyond the scope of this book. For more information, see our website at http://ljpr.com/white-papers or contact our office at (248) 641-7400.

With a type of an IRA called a "Conduit IRA," you can roll all or part of a 401(a) into another plan other than an IRA. For example, say Dave has a Sub-S corporation that he runs a small business through. Dave sets up a 401(a) plan in his company for himself and his employees (which could include his wife and kids of age). He could also roll his 401(a) into his company's qualified 401(a) plan. 401(a) plans allow you to keep contributing if you have income. In addition, 401(a) plans allow a penalty-free distribution after age 55 (as long as you are separated from service), as opposed to 59½ in an IRA.

A Law Enforcement Officer or Firefighter can now also now use a conduit IRA to get all or part of a 401(a) into another 401(a) or other qualified plan. A conduit IRA is a Rollover IRA that only holds a distribution from a qualified plan. For example, Sue retired at 51 and transfers her 401(a) into a Rollover IRA. She does not mingle the rollover with any other IRAs. Two years after retirement, Sue sets up a single-owner LLC to run her real estate business. She sets up a 401(a) plan to defer taxes. She can roll her conduit IRA into her 401(a) plan. She can now manage her funds in one place, and can take penalty free withdrawals of any size in the year she turns 55 instead of 59 ½.

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Years and Ages. There are two types of age determinations for retirement. The 'hard rule' applies to age 59½. If the law states penalties on distributions prior to 59½, the law means exactly when you turn 59½. For the age 50 special exemption for the Law Enforcement Officers and the age 55 exemption for the non-IRA business type plans, the rule is 'the year of.' Thus, a Law Enforcement Officer or Firefighter is not penalized if they get a DC distribution in the year they turn 50. For the 70½ rule, it's weirder. You have to take an RMD not later than April 1st of the year after you turn 70½ (which unfortunately results in you possibly taking two distributions in the year after you turn 70½).

Chapter 3: Withdrawal Checklist

Understand tax rules?

- ❑ §457 rules?
- ❑ 401(a) rules
- ❑ Rollover rules?
- ❑ 72(t) rules?
- ❑ Age 59 ½ penalty?
- ❑ Age 70 ½ penalty?
- ❑ Special exception for separation from service and age 50?

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Chapter 4
Guide to Naming Beneficiaries

Who gets your IRA when you croak (the legal term for dying)? So far, the discussion of DC rollovers has covered how to fund your DC rollover with the lowest tax, how to determine an effective withdrawal strategy, and how to invest your DC rollover effectively. The next issue is to make sure the DC rollover goes to the people you like when you die. This is accomplished through the proper use of a beneficiary designation. Beneficiary designations are one of the most overlooked areas in Law Enforcement Officer and Firefighter retirements.

We've seen all kinds of goof-ups ranging from only naming one beneficiary (hate to tell you this, but your beneficiaries will die too, eventually, and maybe before you) to forgetting to take ex-wives or ex-husbands off a designation. How you look at a beneficiary designation can be addressed by a series of 'then what happens?' questions:

1. "What happens to your DC rollover when you die?" This is the first question and fortunately the one most people can answer.
2. "Then what happens if your primary beneficiary dies before you?" Kids? Grandkids? Charity?
3. "Then what happens?" What if a child predeceases you? To the other children? Grandchildren?

In other words, we suggest your beneficiary designations should be bulletproof, or close to it. You should have it arranged so all options are met. For example, a beneficiary designation might look like this:

Primary:	Spouse 100%
Secondary:	Child one, 50% or their issue by right of representation.
	Child two, 50% or their issue by right of representation.
	With the survivor taking if there is no surviving issue.

This one at least covers the same bases:

- The spouse, if he or she survives,
- The kids equally if the spouse doesn't survive,
- The grandkids or surviving kid of the spouse and kid(s) don't survive: that's what 'issue by right of representation' means.

Taxes to beneficiaries. The taxes to the beneficiaries are dependent on who gets the DC rollover, a spouse or a non-spouse.

Spouse. A spouse who gets a DC rollover can do a 'spousal rollover' and turn the DC rollover or Rollover IRA into his/her own IRA. From that point, the new Rollover IRA is the spouse's and subject to his/her beneficiary designations and Required Minimum Distribution rules (remember that stuff about age 70½).

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Non-Spouse (i.e. kids or grandkids). Non-spouse beneficiaries who inherit a DC or IRA Rollover receive it in an 'Inherited IRA.' If the beneficiaries designated are individuals and are distributed a percentage of the DC or IRA Rollover (as opposed to a dollar amount), they may take the distribution over a period of time. The longest period a non-spouse can take distributions from an Inherited IRA is over their life expectancy (from the IRS tables). They also have the option of taking the money sooner. Non-spouse beneficiaries pay taxes on any distributions. Note: new rules make Inherited IRAs subject to the claims of creditors. So if your children inherit your IRA, the IRA can be subject to lawsuits against them (and potentially their spouse as well). This can be protected with IRA Trust. See your attorney or call us if you have questions about IRA Trusts.

Estate. If the DC owner fails to name a beneficiary, or the named beneficiaries don't survive, then the DC or IRA Rollover will go to their estate. This is bad for a variety of reasons. For example, the IRA is now subject to probate and the funds must be disbursed (and taxed) within five years of the owner's death.

Trust. Simply naming a Trust as a beneficiary would seem a solution, but there is a technical issue (don't you love lawyers?). For a Trust to effectively distribute an IRA of the longest possible period, it needs to have some very specific provisions to direct the "flow-through" of the IRA distributions to the beneficiaries. Many times, when you want to pass an IRA on to grandchildren or younger (or immature older) children, you can use a special IRA Trust as a beneficiary.

Charity. A charity can be named an IRA beneficiary. Charities are tax-exempt and passing an IRA to the charity avoids income tax. For people with big estates, leaving an IRA to charity can reduce both income taxes and estate taxes. Be careful if you are leaving an IRA to both a charity and individuals—specific IRS rules must be followed. It's usually preferable to open a separate IRA for the charitable bequest.

Chapter 4: Beneficiaries Checklist

- ❑ Have primary beneficiary for every plan?
    - §457?
    - 401(a)?
    - DROP rollover?
    - IRAs?
    - Roth IRAs?
- ❑ Have secondary and contingent beneficiary for every plan?
    - §457?
    - 401(a)?
    - DROP rollover?
    - IRAs?
    - Roth IRAs?
- ❑ Using best beneficiary to stretch payout?
- ❑ Naming charity beneficiaries the right way?
- ❑ Have beneficiary designation worded correctly?

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Conclusion

DC and Deferred Comp are very important ingredients in your future retirement security. You need to pay close attention to the three aspects of DC and Deferred Comp:

- **Making Contributions**. Go back through the contribution section and make some calculations on how you can maximize your contributions. Remember, at the beginning, it's how much you contribute that counts. And we think free money is good money.
- **Investing.** Review the section on investing and consider that once you hit 'critical mass,' your DC or Deferred Comp is adding more to the balance than your contributions. At that juncture, you need to pay close attention to how you invest your funds. Now you need to pay close attention to the mix (remember, that is the most important factor), the ingredients, and your style of investing. Also recall that you need to rebalance to reduce risk and you might increase returns as well. If you need a professional, unbiased, non-commissioned look at your investments, fill out the information request form at the end of the book, or call us at 248.641.7400.
- **Withdrawals.** You put it in, you invested it, and now you can take it out. Go review the withdrawal section to see what sustainable withdrawals can be, and the important aspects of taxes on your withdrawals strategy.

DC and Deferred Comp can build some significant retirement money (we've seen well over $1 million). With great opportunity comes responsibility. If you want to make a DC or Deferred comp plan work at its best, you have to pay attention to how much you put in, how you invest it and how you take it out. All in all, you can build a retirement with DC and Deferred Comp (we have 401(a), which is the equivalent of Deferred Comp). But pay attention, something as a Michigan Law Enforcement Officer or Firefighter, you're used to.

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About Us:

Leon C. LaBrecque, JD, CPA, CFP®, CFA is the CEO and Chief Strategist at the independent advisory firm, LJPR, LLC. **Matthew Teetor** is a Financial Advisor and Principal in the firm. LJPR reduces uncertainty for Michigan police officers and firefighters and their families by applying creative wealth management solutions in tax, financial planning, retirement planning and estate planning. To contact us for a consultation or to discuss your financial situation, email **guns.hoses@ljpr.com** or call 248.641.7400. Also visit our blog and website, including our Guns & Hoses page devoted to Michigan law enforcement officers and firefighters at **ljpr.com/about-g&h**.

For a free consultation on your employer retirement plan, call our office, or send an email to **guns.hoses@ljpr.com**.

See the appendix for a current summary of some of the funds available to Michigan Law Enforcement offers and Firefighters in their municipal retirement accounts.

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Appendix | Summary of Funds*

Manager	Category	Expense Ratio	Inception Date
Great West			
Aggressive Profile	Aggressive Allocation	1.22%	9/1/1997
Moderately Aggressive Profile	Aggressive Allocation	1.12%	9/1/1997
Great-West Guaranteed Fixed Fund	Annuity	-	-
Moderately Conservative Portfolio	Conservative Allocation	0.90%	9/1/1997
Conservative Portfolio	Conservative Allocation	0.83%	9/1/1997
Federated Capital Appreciation	Conservative Allocation	1.34%	5/1/2002
Artisan International Fund	Foreign Large Blend	1.23%	7/1/2000
Maxim MFS International Growth	Foreign Large Growth	1.20%	7/1/2009
Maxim Invesco ADR Portfolio	Foreign Large Value	1.12%	11/1/1994
Maxim Ariel Small-Cap Value	Foreign Small/Mid Value	1.39%	12/1/1993
Maxim MFS International Value Portfolio	Foreign Stock	1.18%	12/1/1993
Putnam High Yield Advantage R	High Yield Bond	1.29%	5/1/2008
Putnam International Capital Opportunity	High Yield Bond	1.87%	5/1/2008
Maxim US Government Securities	Intermediate Government	0.60%	12/1/1993
Maxim Bond Index Portfolio	Intermediate Term Bond	0.50%	9/1/1999
Maxim Federated Bond Portfolio	Intermediate Term Bond	0.70%	7/1/2009
Pimco Total Return	Intermediate-Term Bond	0.72%	5/1/2002
Maxim S&P 500 Index	Large Blend	0.60%	9/1/2003
Maxim Stock Index Portfolio	Large Blend	0.60%	1/1/1992
Davis New York Venture Fund	Large Blend	1.23%	8/1/2006
Maxim Janus Large Cap Growth	Large Growth	1.05%	7/1/2009
Oppenheimer Capital Appreciation	Large Growth	1.19%	8/1/2001
American Funds Growth Fund of America	Large Growth	0.97%	8/1/2006
Maxim American Century Growth Portfolio	Large Growth	-	5/1/2011
Maxim T. Rowe Price Equity/Income Port	Large Value	0.83%	12/1/1994
American Century Equity Income Fund	Large Value	0.97%	9/1/1999
INVESCO Van Kampen Comstock Fund	Large Value	1.11%	8/1/2006
Ariel Appreciation Fund	Mid-Cap Blend	1.18%	1/1/1992
Lord Abbett Value Opportunities	Mid-Cap Blend	1.34%	7/1/2009
Maxim T. Rowe Price MidCap Growth	Mid-Cap Growth	1.05%	7/1/1997
Columbia Mid Cap Value Equity	Mid-Cap Value	1.44%	5/1/2008
Ridgeworth Mid-Cap Value	Mid-Cap Value	1.05%	5/1/2011
INVESCO Van Kampen American Value	Mid-Cap Value	1.57%	5/1/2008
Moderate Profile	Moderate Allocation	0.98%	9/1/1997
Maxim Loomis Sayles Bond Portfolio	Multi-Sector Bond	0.90%	1/1/1995
Maxim Index 600 Portfolio	Small Blend	0.60%	1/1/1994
Maxim Loomis Sayles Small Cap Value	Small Blend	1.12%	11/1/1994
Royce Total Return	Small Blend	1.46%	5/1/2008
RidgeWorth Small Cap Growth Stock	Small Growth	1.22%	5/1/2005
Maxim Lifetime 2015 Portfolio II	Target Date 2011-2015	0.88%	5/1/2009
Maxim Lifetime 2025 Portfolio II	Target Date 2020-2025	0.95%	5/1/2009
Maxim Lifetime 2035 Portfolio II	Target Date 2030-2035	1.00%	5/1/2009
Maxim Lifetime 2045 Portfolio II	Target Date 2040-2045	1.01%	5/1/2009
Maxim Lifetime 2055 Portfolio II	Target Date 2051+	1.02%	5/1/2009
Maxim Templeton Global Bond	World Bond	1.30%	7/1/1999
Oppenheimer Global Fund	World Stock	1.20%	7/1/2004
ICMA			
VT Vantagepoint MP Long-Term Growth	Aggressive Allocation	0.89%	4/1/1996
VT Vantagepoint MP Conservative Growth	Conservative Allocation	0.84%	4/1/1996
VT Vantagepoint International	Foreign Large Blend	0.98%	10/1/1994
VT Vantagepoint Overseas Equity Index	Foreign Large Blend	0.52%	4/5/1999
VT Fidelity Diversified International	Foreign Large Blend	1.01%	12/27/1991
VT Harbor International	Foreign Large Blend	1.14%	11/1/2002
VT PIMCO High Yield	High Yield Bond	0.90%	1/16/1995

VT Vantagepoint Inflation Protection	Inflation Protected Bond	0.63%	7/1/1992
VT Vantagepoint Core Bond Index	Intermediate Term Bond	0.40%	4/5/1999
VT Pimco Total Return	Intermediate Term Bond	0.55%	9/7/1994
VT Vantagepoint MP All-Equity Growth	Large Blend	0.97%	10/1/2000
VT Vantagepoint 500 Stock Index	Large Blend	0.41%	4/5/1999
VT Vantagepoint Broad Market	Large Blend	0.42%	4/5/1999
VT Vantagepoint Growth and Income	Large Blend	0.78%	10/2/1998
VT Oppenheimer Mainstreet	Large Blend	0.97%	11/1/1996
VT Vantagepoint Growth	Large Growth	0.54%	4/1/1983
VT Fidelity Contrafund	Large Growth	0.74%	5/17/1967
VT Calvert Equity Portfolio	Large Growth	1.22%	8/24/1987
VT T Rowe Price Growth Stock	Large Growth	0.70%	12/31/2001
VT Vantagepoint Equity Income	Large Value	0.82%	4/1/1994
VT Eaton Vance Large-Cap	Large Value	0.99%	9/23/1931
VT Allianz NFJ Dividend Value	Large Value	1.06%	5/8/2000
VT Vantagepoint MD/SM Cap Equity	Mid-Cap Blend	0.42%	4/5/1999
VT Vantagepoint Aggressive Opps	Mid-Cap Growth	0.85%	10/1/1994
VT Harbor Mid Cap Growth	Mid-Cap Growth	1.10%	11/1/2002
VT Royce Premier	Mid-Cap Growth	2.05%	9/17/2002
VT Rainier Small/Mid Cap Equity	Mid-Cap Growth	0.99%	5/10/1994
VT Vantagepoint Select Value	Mid-Cap Value	0.99%	10/30/2007
VT Goldman Sachs Mid Cap Value	Mid-Cap Value	1.15%	8/15/1997
VT Columbia Mid Cap Value	Mid-Cap Value	1.20%	11/20/2001
VT Vantagepoint MP Traditional Growth	Moderate Allocation	0.86%	4/1/1996
VT Fidelity Puritan	Moderate Allocation	0.58%	4/16/1947
VantageTrust PLUS Fund	Money Market	-	1/1/1991
Vantage Trust Cash Management	Money Market	-	3/1/1999
VT Nuveen Real Estate Securities	Real Estate	1.28%	6/30/1995
VT Retirement Income Advantage	Retirement Income	0.83%	8/23/2010
VT Vantagepoint MS Ret Income	Retirement Income	0.58%	1/3/2005
VT Vantagepoint MP Savings Oriented	Retirement Income	0.58%	2/9/1995
VT Vantagepoint Discovery	Small Blend	0.97%	10/30/2007
VT T Rowe Price Sm-Cap Value	Small Blend	0.98%	3/31/2000
VT Royce Value Plus	Small Growth	1.06%	6/14/2001
VT Vantagepoint Milestone 2010	Target Date 2011-2015	0.62%	1/3/2005
VT Vantagepoint Milestone 2015	Target Date 2015-2020	0.85%	1/3/2005
VT Vantagepoint Milestone 2020	Target Date 2020-2025	0.84%	1/3/2005
VT Vantagepoint Milestone 2025	Target Date 2025-2030	0.85%	1/3/2005
VT Vantagepoint Milestone 2030	Target Date 2030-2035	0.86%	1/3/2005
VT Vantagepoint Milestone 2035	Target Date 2035-2040	0.87%	1/3/2005
VT Vantagepoint Milestone 2040	Target Date 2040-2045	0.88%	1/3/2005
VT Vantagepoint Milestone 2045	Target Date 2045-2050	0.97%	1/4/2010
	Nationwide		
Nationwide Investor Destination Moderate Aggressive	Aggressive Allocation	0.86%	3/30/2000
NW Alternative Allocation	Conservative Allocation	1.16%	7/25/2011
Nationwide Investor Destination Conservative	Conservative Allocation	0.88%	3/30/2000
Nationwide Investor Destination Moderate Conservative	Conservative Allocation	0.87%	3/30/2000
Blackrock Natural Resources Trust	Equity Energy	1.13%	10/21/1994
American Funds EuroPacific Growth	Foreign Large Blend	1.14%	4/16/1984
American Funds American High Imcome	High Yield Bond	1.03%	2/19/1988
Pimco Total Return	Intermediate Term Bond	0.85%	5/11/1987
Dreyfus Appreciation Fund	Large Blend	0.97%	1/18/1984
Nationwide S&P 500 Index	Large Blend	0.61%	7/24/1998
Davis NY Venture	Large Blend	0.90%	2/17/1969
Nationwide Investor Destination Aggressive	Large Blend	0.87%	3/30/2000
Neuberger Berman Social Responsibility	Large Growth	1.06%	3/16/1994
Trowe Price Growth Stock	Large Growth	1.20%	4/11/1950
American Funds Growth Fund of America	Large Growth	0.98%	11/30/1973
Nationwide Growth	Large Growth	1.27%	2/14/1961
Nationwide Large Cap Growth	Large Growth	0.95%	4/27/2007

Invesco Growth and Income	Large Value	0.84%	8/1/1946
Oppenheimer Value	Large Value	0.95%	9/16/1985
Eaton Vance Build America Bond	Long-Term Bond	1.14%	11/17/2009
Nationwide Mid Cap Market Index	Mid-Cap Blend	0.71%	12/29/1999
American Century Heritage	Mid-Cap Growth	1.26%	11/10/1987
Goldman Sachs Mid-Cap	Mid-Cap Value	1.15%	8/15/1997
Nationwide Investor Destination Moderate	Moderate Allocation	0.86%	3/30/2000
Nationwide Money Market	Money Market-Taxable	0.48%	3/3/1980
American Century Real Estate A	Real Estate	1.40%	9/21/1995
Nationwide Retirement Income	Retirement Income	0.71%	8/29/2007
Oppenheimer Main Street Small Cap	Small Blend	1.24%	8/2/1999
Legg Mason Small Cap Growth	Small Growth	1.32%	7/1/1998
JP Morgan Small Cap Value	Small Value	1.42%	6/30/1972
American Beacon Small Cap Value Advisor	Small Value	1.42%	12/31/1998
Nationwide Destination 2015	Target Date 2011-2015	0.70%	8/29/2007
Nationwide Destination 2020	Target Date 2015-2020	0.69%	8/29/2007
Nationwide Destination 2025	Target Date 2020-2025	0.69%	8/29/2007
Nationwide Destination 2030	Target Date 2025-2030	0.68%	8/29/2007
Nationwide Destination 2035	Target Date 2030-2035	0.68%	8/29/2007
Nationwide Destination 2040	Target Date 2035-2040	0.68%	8/29/2007
Nationwide Destination 2045	Target Date 2040-2045	0.68%	8/29/2007
Nationwide Destination 2050	Target Date 2045-2050	0.68%	8/29/2007
Nationwide Destination 2055	Target Date 2051+	0.61%	12/27/2010
American Funds Capital World Growth and Income	World Stock	1.10%	3/26/1993

*Fund options may vary depending on your plan and plan provider. Always seek professional advice when picking funds.

Disclosures

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