IDAHO

PERSpectives

First Quarter 2011 Public Employee Retirement System of Idaho

THE 2011 SOCIAL SECURITY TAX REDUCTION

Through 2011, the payroll tax (FICA) portion of your paycheck tax withholding — which funds Social Security and Medicare — will be cut by 2 percent. You may have noticed the withholding rates for your Social Security taxes have already dropped from 6.2 percent to 4.2 percent. (The other 1.45 percent of your FICA tax that funds Medicare will remain unchanged.)

How Does the Tax Cut Work?

Social Security tax generally takes 6.2 percent of the first $106,800 of a worker's wages. For most people, that means 6.2 percent of every dollar earned. The 2011 payroll tax "holiday" reduces the rate to 4.2 percent, so most workers will automatically have more in their paychecks.

> For example: If your annual income is $50,000, you are paid biweekly, and you don't put money away in any flexible spending accounts, your check could increase by as much as $38 per pay period (or $76 a month more in net pay).

The Social Security tax payments stop when a worker's wages hit $106,800; this tax cut tops out at $2,136 for a single wage earner and at $4,272 for a married couple where both workers have six-figure salaries. Unlike many tax breaks, this break does not disappear for higher-income earners.

Here is a link to Kiplinger's website for a calculator to determine the increase in your take home pay.
http://www.kiplinger.com/tools/2011_Social_Security_payroll_tax_cut_calculator/

Not Everyone Gets the Break

Not everyone will benefit from this tax holiday.

> For example: Retirees who don't get a paycheck from an employer, and some federal and state workers who are covered by a retirement plan other than Social Security, will not benefit from this tax break.

But most Americans will have more money to spend, save, or pay off debts.

What to Do with the Money?

Although this tax cut was designed to stimulate the economy, not everyone will go out and spend the money as the government and businesses hope. There are several options for using your "windfall" other than spending it.

Saving for Retirement

By now, your employer has begun withholding less for your Social Security taxes, leaving more for you. PERSI members should consider contributing this 2 percent tax savings to either a new or existing PERSI Choice 401(k) Plan account. If you can't contribute all 2 percent, consider deferring 1 percent into an account. There would be little difference in your net pay, but there could be a big difference to you at retirement. If you are not currently a Choice 401(K) Plan participant, complete an deferral election form (RS-801) and submit it to your payroll department. You can also request an enrollment kit from the PERSI website using this link:
www.persi.idaho.gov/members/choice_401k_plan.cfm

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Insights

TOO MUCH INFORMATION AND TOO MANY CHOICES?

Studies show defined contribution plan participants who get too much information or who are given too many investment choices, can be overwhelmed. Providing as many choices as possible may sound like a good idea, but research has shown having too many investment options can actually hinder participation, even paralyze decision-making.

Some plan sponsors think offering 25, 50, or even 100 options will enhance participation. A study by Vanguard on 401(k) enrollment found for every 10 additional options, the number of employees who enrolled dropped by 2 percent. When given only two choices, participation was at 75 percent; but when that number increased to 60 options, the participation rate dropped to 60 percent. It's difficult to choose from among so many funds, therefore many people give up. The average plan offers 18 options; but experts agree the optimal number of choices is somewhere between 8-12.

The larger the number of investment options, the more time the plan sponsor and participants need to spend on education...and that's not how participants want to spend their time according to researchers. Studies show it's not just less knowledgeable participants who are overwhelmed, but "sophisticated" participants find too many choices just as confusing. The William and Mary School of Business Administration gave 398 participants a written financial literacy test. Out of a possible 10, the average score on the test was less than 4. Not surprisingly, the study found "less knowledgeable participants (those scoring below average) were overwhelmed regardless of whether they had relatively few or many investment options" from which to choose. The study also found the "knowledgeable" participants (those scoring above average and the group that might be expected to benefit from more investment choices) were more likely to use the default investment option when the number of choices increased. The conclusion by William and Mary was that participants at all levels needed additional financial education and that reducing the number of options did little to lower the overload even on "individuals with above average financial knowledge." The problem is obvious according to the study: Most participants do not know how to effectively manage their investment accounts. (*This lack of investing knowledge has been part of the national debate about switching pensions from defined benefit plans manage by professional investors to self-managed defined contribution plans.)*

Another interesting observation from a study conducted by Columbia University, showed "a significant number of investment choices motivated participants to choose less risky investments." The reason for this, participants recognize they are not experts...they think "this isn't what I do, there are too many options, so I'll play it safe." This could be a costly allocation decision for participants who are a long way from retirement. It's important for plans to offer a fund menu that enables participants to develop the appropriate allocation based on personal goals, risk tolerance, and years until retirement.

So, what does all this mean to PERSI members? It means PERSI understands that choice is not only powerful but can also be overwhelming; therefore, members are provided with understandable educational materials about the Choice 401(k) Plan, and particpation is made easy. The Choice Plan offers 12 investment options within three main categories: **Balanced, Equity,** and **Fixed Income**. The default option for the Choice Plan is the PERSI Total Return Fund, used for investing Base Plan funds...which as of this writing has fiscal year-to-date returns of 18.0 percent.

PERSI encourages members to plan for their retirement by participating in plans to supplement their Base Plan and Social Security retirement benefits. PERSI deliberately limits investment options for the Choice Plan to a core number of funds participants can understand. By providing clear and simple materials about the investment options available and educating members about the advantages of saving for retirement, most participants should be able to make better decisions...and perhaps enjoy a more secure retirement.

RETIREMENT MISCONCEPTIONS

Two big misconceptions or outdated ideas about retirement still exist, even among individuals who have attended retirement workshops or educated themselves on what to expect when they stop working.

Assuming a Short Retirement

Life expectancy goes far beyond previous generations. Today, Americans are expected to live into their 90s. Most of us imagine retirement much like the life we live during our working years, except with more control over how we spend our time. We want our retirement resources to last throughout our "golden years," yet many of us don't plan for a 20-, 25-, or 30-year retirement.

In 2010, the American Academy of Actuaries said the average 65-year-old American man could expect to live to 84½, with a 30 percent chance of living past 90. The average 65-year-old American woman has an average life expectancy of 87, with a 40 percent chance of living past 90. If your financial plan does not consider a longer life expectancy, you could outlive your money.

Your Base Plan and Social Security benefits were never meant to replace 100 percent of your income when you stop working. The average Social Security monthly benefit is $1177 and the average PERSI retirement benefit is $1342. This might sound good to many people, but it may not be enough for a stable retirement for many others. A third (or even fourth) retirement savings account provides more retirement security.

If you haven't started contributing to a supplemental retirement savings account, such as the Choice 401(k) Plan, it's not too late to get started. It can make an impact on your quality of life in retirement. To begin making contributions to the Choice 401(k) Plan account, complete the deferral election form available on the PERSI website (http://www.persi.idaho.gov/forms/RS801.pdf) and return it to your payroll clerk.

Assuming Too Little Risk

As we age, conservative investing is not mandatory. Given how long people are living and the average length of retirement, it is important to have investments with growth potential. Consider reviewing your investments with a financial advisor to get a better understanding about what you'll need for income when you retire.

What Will Impact Your Retirement?

Three things can impact your retirement savings — ***inflation***, ***taxes*** *and* ***health care costs***.

Although current inflation is low, even moderate inflation can affect purchasing power in retirement. If you are nearing retirement, think about what it would be like to live on the same income for 10 years as prices rise and your dollar buys less. Inflation is a fact of life workers have historically dealt with through pay increases, but after retirement few people can increase their income enough to keep pace with the cost of living. [PERSI offers cost-of-living-adjustments to its retirees (subject to legislative approval) to help in this area.]

Taxes continue to change, taking a bigger chunk of your money each year. Evaluating your retirement plan and reviewing your investment accounts with a professional — even if you are in your 20s or 30s, and most certainly if you are in your 40s or 50s — makes good sense if you want to get the most from your retirement money and reduce your taxes.

Health care costs seem to rise each year. It's never too early (or too late) to start learning about the cost of health care premiums in retirement, to identify what kind of coverage will meet your needs, and to prepare for the cost of acute, chronic, and long-term care. Now is the time to adjust your retirement savings to accommodate your future needs.

While it's still early in the year, take a look at your qualified retirement plans (IRA, 401(k), etc.), and set a retirement savings goal to put you on the right path towards a comfortable retirement. (Be sure to review your annual Base Plan statement that comes out each fall and your Choice 401(k) Plan annual statement that arrives in January.) Don't wake up one day to find you're not financially ready for retirement.

Social Security continued from page 1

Pay Down Debt

If you have high interest credit cards or other loan balances, you might want to use your 2 percent "government gift" and apply it to that debt. With more money in your pocket, you can adjust your monthly payment upward by the additional 2 percent you are getting from the federal government. This paydown approach can be applied to your car payment as well. Just make sure the extra money is applied to paying down the principal.

Make an Extra Mortgage Payment

Your 2011 tax break might be enough to make a 13th mortgage payment. Again, be sure your lender applies the extra payment to the principal balance.

The government hopes individuals will spend the extra money to boost the economy. Ideas presented in this article may not support spending your extra money, but maximizing every dollar you have — whether you increase your retirement savings or pay off debt — is never a bad idea.

PERSI WEBSITE UNDERGOES CHANGE

The PERSI website will soon have a new look. Graphic elements have been used to tie the website more closely to those of other state agencies. PERSI blended existing features with new design elements suggested by the state. The result is a clean and easy-to-use website that has a feel similar to other state entities.

The most noticeable changes are the state seal and color palette. PERSI is adding a news ticker that streams updates -- the movement is eye-catching, but not so much that it distracts from other parts of the home page. The actual layout is not changing much, so members who visited the PERSI website in the past should feel comfortable navigating the updated site.

www.persi.idaho.gov

PERSI INVESTMENT NEWS

as of March 25, 2011

Value of the Fund:
$11,793,521,357

Fiscal Year Change in Market Value:
$ 1,715,496,852

Fiscal Year-to-Date Returns:
18.0%

Month-to-Date Returns:
0.1%

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