City State Bank Trusts & Investments
Fall 2017 Newsletter

CITY STATE BANK INVEST

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FOUR NUMBERS YOU NEED TO KNOW NOW

When it comes to your finances, you might easily overlook some of the numbers that really count. Here are four to pay attention to now that might really matter in the future.

1. RETIREMENT PLAN CONTRIBUTION RATE

What percentage of your salary are you contributing to a retirement plan? Making automatic contributions through an employer-sponsored plan such as a 401(k) or 403(b) plan is an easy way to save for retirement, but this out-of-sight, out-of-mind approach may result in a disparity between what you need to save and what you actually are saving for retirement. Checking your contribution rate and increasing it periodically can help you stay on track toward your retirement savings goal. Some employer retirement plans let you sign up for automatic contribution rate increases each year, which is a simple way to bump up the percentage you're saving over time. In addition, try to boost your contributions when you receive a pay raise. Consider contributing at least enough to receive the full company match (if any) that your employer offers.

2. CREDIT SCORE

When you apply for credit, such as a mortgage, a car loan, or a credit card, your credit score is one of the tools used by lenders to evaluate your creditworthiness. Your score will likely factor into the approval decision and affect the terms and the interest rate you'll pay. The most common credit score that creditors consider is a FICO© Score, a three-digit number that ranges from 300 to 850. This score is based on a mathematical formula that uses information contained in your credit report. In general, the higher your score, the lower the credit risk you pose. Each of the three major credit reporting agencies (Equifax, Experian, and TransUnion) calculates FICO® scores using different formulas, so you may want to check your scores from all three (fees apply). You're entitled to one free copy of your credit report every 12 months from each of the three credit reporting agencies. You can get your copy by visiting annualcreditreport.com.

3. DEBT-TO-INCOME RATIO

Your debt-to-income ratio (DTI) is another number that lenders may use when deciding whether to offer you credit. A DTI that is too high might mean that you are overextended. Your DTI is calculated by adding up your major monthly expenses and dividing that figure by your gross monthly income. The result is expressed as a percentage. For example, if your monthly expenses total $2,200 and your gross monthly income is $6,800, your DTI is 32%. Lenders decide what DTIs are acceptable, based on the type of credit. For example, mortgage lenders generally require a ratio of 36% or less for conventional mortgages and 43% or less for FHA mortgages when considering overall expenses. Once you know your DTI, you can take steps to reduce it if necessary. For example, you may be able to pay off a low-balance loan to remove it from the calculation. You may also want to avoid taking on new debt that might negatively affect your DTI. Check with your lender if you have any questions about acceptable DTIs or what expenses are included in the calculation.

4. NET WORTH

One of the key big-picture numbers you should know is your net worth, a snapshot of where you stand financially. To calculate your net worth, add up your assets (what you own) and subtract your liabilities (what you owe). Once you know your net worth, you can use it as a baseline to measure financial progress. Ideally, your net worth will grow over time as you save more and pay down debt, at least until retirement. If your net worth is stagnant or even declining, then it might be time to make some adjustments to target your financial goals, such as trimming expenses or rethinking your investment strategy.

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CITY STATE BANK TRUST & INVESTMENTS

IS IT WISE TO TRADE YOUR PENSION FOR A LUMP SUM?

About 41 million people are participants (active, retired, or separated vested) of PBGC-insured corporate pension plans.

Source: Congressional Budget Office, 2016

Most private employers have already replaced traditional pensions, which promise lifetime income payments in retirement, with defined contribution plans such as 401(k)s. But 15% of private-sector workers and 75% of state and local government workers still participate in traditional pensions.[1] Altogether, 35% of workers say they (and/or their spouse) have pension benefits with a current or former employer.[2]

Many pension plan participants have the option to take their money in a lump sum when they retire. And since 2012, an increasing number of large corporate pensions have been implementing "lump-sum windows" during which vested former employees have a limited amount of time (typically 30 to 90 days) to accept or decline buyout offers.[3] (Lump-sum offers to retirees already receiving pension benefits are no longer allowed.)

By shrinking the size of a pension plan, the company can reduce the associated risks and costs, and limit the impact of future retirement obligations on current financial performance. However, what's good for a corporation's bottom line may or may not be in the best interests of plan participants and their families. For many workers, there may be mathematical and psychological advantages to keeping the pension. On the other hand, a lump sum could provide financial flexibility that may benefit some families.

WEIGH RISKS BEFORE LETTING GO

A lump-sum payout transfers the risks associated with investment performance and longevity from the pension plan sponsor to the participant. The lump-sum amount is the discounted present value of an employee's future pension, set by an IRS formula based on current bond interest rates and average life expectancies.

Individuals who opt for a lump-sum payout must then make critical investment and withdrawal decisions, and determine for themselves how much risk to take in the financial markets. The resulting income is often not enough to replace the pension income given up, unless the investor can tolerate exposure to stock market risk and is able to achieve solid returns over time. Gender is not considered when calculating lump sums, so a pension's lifetime income may be even more valuable for women, who tend to live longer than men and would have a greater chance of outliving their savings.

In addition, companies might not include the value of subsidies for early retirement or spousal benefits in lump-sum calculations.[4] The latter could be a major disadvantage for married participants, because a healthy 65-year-old couple has about a 73% chance that one spouse will live until at least 90.[5]

WHEN A LUMP SUM MIGHT MAKE SENSE

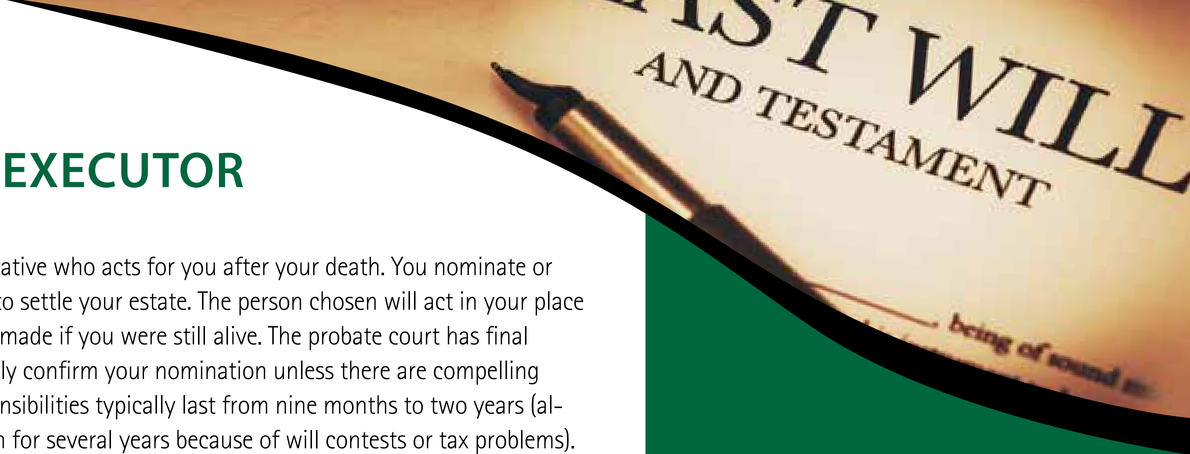
A lump-sum payment could benefit a person in poor health or provide financial relief for a household with little cash in the bank for emergencies. But keep in mind that pension payments (monthly or lump sum) are taxed in the year they are received, and cashing out a pension before age 59½ may trigger a 10% federal tax penalty.[6] Rolling the lump sum into a traditional IRA postpones taxes until withdrawals are taken later in retirement. Someone who expects to live comfortably on other sources of retirement income might also welcome a buyout offer. Pension payments end when the plan participant (or a surviving spouse) dies, but funds preserved in an IRA could be passed down to heirs.

IRA distributions are also taxed as ordinary income, and withdrawals taken prior to age 59½ may be subject to the 10% federal tax penalty, with certain exceptions. Annual minimum distributions are required starting in the year the account owner reaches age 70½.

It may also be important to consider the health of the company's pension plan, especially for plans that don't purchase annuity contracts. The "funded status" is a measure of plan assets and liabilities that must be reported annually; a plan funded at 80% or less may be struggling. Most corporate pensions are backstopped by the Pension Benefit Guaranty Corporation (PBGC), but retirees could lose a portion of the "promised" benefits if their plan fails.

The prospect of a large check might be tempting, but cashing in a pension could have costly repercussions for your retirement. It's important to have a long-term perspective and an understanding of the tradeoffs when a lump-sum option is on the table.

[1] U.S. Bureau of Labor Statistics, 2016
[2] Employee Benefit Research Institute, 2016
[3, 4] *The Wall Street Journal*, June 5, 2015
[5] Society of Actuaries, 2017
[6] The penalty doesn't apply to employees who retire during or after the year they turn 55 (50 for qualified public safety employees).



SELECTING AN EXECUTOR

WHAT IS AN EXECUTOR?

An executor is a personal representative who acts for you after your death. You nominate or designate an executor in your will to settle your estate. The person chosen will act in your place to make decisions you would have made if you were still alive. The probate court has final approval, but the court will generally confirm your nomination unless there are compelling reasons not to. An executor's responsibilities typically last from nine months to two years (although, an estate may remain open for several years because of will contests or tax problems).

The functions of an executor are varied, but generally your executor:

- Locates and probates your will
- Inventories, collects, and sells (if necessary) your assets
- Pays legitimate creditor claims
- Pays any taxes owed by your estate
- Distributes any remaining assets to your beneficiaries

Your executor is entitled to a fee from your estate for services rendered.

WHAT ARE THE DUTIES OF AN EXECUTOR?

Your executor acts in a fiduciary capacity. This means that he or she must exercise a high degree of care at all times. Additionally, your executor is under court supervision, subject to its control and approval.

Some states require executors to post a bond, which is later paid back to the executor from the estate (though you may be able to waive this requirement through a will provision). In addition, your executor is personally responsible for ensuring that all the proper tax returns are filed and that any estate taxes due are paid. Finally, your executor is accountable to the court and to your beneficiaries on completion of his or her duties.

HOW DO YOU SELECT AN EXECUTOR?

Your choice of executor is a very important one. Ideally, you want someone you can trust, who has a close relationship to your family, who has some understanding of tax laws, and who has a keen sense of business (especially if you are a business owner).

You can name multiple executors to oversee different aspects of your affairs. However, coexecutors may result in an increase in paperwork and a slowdown in the probate process. Some of the attributes you should look for in a good executor are:

- Ability to serve
- Willingness to serve
- Competency
- Trustworthiness
- Appreciation of your family's needs
- Knowledge and experience

INDIVIDUAL VERSUS PROFESSIONAL

When choosing an executor, you can name an individual or a professional (e.g., a bank trust department) to handle your affairs.

A family member or close friend has knowledge of your affairs and should take a personal interest in the settlement of your estate and the well-being of your beneficiaries. However, he or she may not be the best choice. Serving as an executor is a time consuming and stressful task. Some of the executor's duties are very demanding: preparing and filing tax returns, obtaining appraisals, making an accurate accounting, and these are things best left to professionals. By naming a professional to manage your affairs, you gain some permanence. A professional who makes money from managing estates will have the investment expertise as well as the legal, tax, accounting, and computer abilities to do the job well and efficiently. You also gain some impartiality by having a professional manage your affairs. A professional executor should be more impartial to your beneficiaries or heirs. You also reduce the risk that your executor will make hardship loans to friends.

Are you listed as an executor for family or friends in their wills? You may have the willingness and knowledge to fulfill this role if you are called to do so, but taking care of kids, parents, job, and other activities might be the things eating up all your time.

Are you worried about family conflict with siblings as executor of your parents will? City State Bank Trust and Investments can assist you by acting as an impartial executor.

Contact us today to learn more.

TRUST & INVESTMENTS

ARE YOU READY TO RETIRE?

Here are some questions to ask yourself when deciding whether or not you are ready to retire.

IS YOUR NEST EGG ADEQUATE? It may be obvious, but the earlier you retire, the less time you'll have to save, and the more years you'll be living off your retirement savings. The average American can expect to live past age 78.* Is your nest egg large enough to fund 20 or more years of retirement?

WHEN WILL YOU BEGIN RECEIVING SOCIAL SECURITY BENEFITS? You can receive Social Security retirement benefits as early as age 62. However, your benefit may be 25% to 30% less than if you waited until full retirement age (66 to 67, depending on the year you were born).

HOW WILL RETIREMENT AFFECT YOUR IRAS AND EMPLOYER RETIREMENT PLANS? The longer you delay retirement, the longer you can build up tax-deferred funds in traditional IRAs and potentially tax-free funds in Roth IRAs. Remember that you need taxable compensation to contribute to an IRA. You'll also have a longer period of time to contribute to employer-sponsored plans like 401(k)s — and to receive any employer match or other contributions. (If you retire early, you may forfeit any employer contributions in which you're not fully vested.)

WILL YOU NEED HEALTH INSURANCE? Keep in mind that Medicare generally doesn't start until you're 65. Does your employer provide post-retirement medical benefits? Are you eligible for the coverage if you retire early? If not, you may have to look into COBRA or an individual policy from a private insurer or the health insurance marketplace — which could be an expensive proposition.

IS PHASING INTO RETIREMENT RIGHT FOR YOU? Retirement need not be an all-or-nothing affair. If you're not quite ready, financially or psychologically, for full retirement, consider downshifting from full-time to part-time employment. This will allow you to retain a source of income and remain active and productive.

Come see us to help you answer any of the above questions.

* NCHS Data Brief, Number 267, December 2016

IMPORTANT DISCLOSURES

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Photo credit Business Record

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