

Enhancing Your Benefits

The re-enrollment period is now coming to an end on most campuses and most of you have already made final decisions on your medical, dental, and vision coverages and the optional coverages for life, accidental death and dismemberment, and long term disability insurance for 2004-5. You should have, by the time you read this, signed and submitted your re-enrollment form for the next plan year. If you have failed to do so by now, contact your payroll/benefits office immediately. Otherwise, you will fall back to the default coverages and you will be unable to make plan changes until the next re-enrollment period. Unless you have a "change in family status" such as a birth, death, separation, divorce, adoption, etc., all of you must live with the consequences of your re-enrollment decisions for the entire upcoming plan year.

At this point it is easy to think that you are done and that, mercifully, you will not have to trouble yourself again about these matters for another year. Yet after the onslaught of these decisions is over and the slower pace of summer approaches, perhaps you have more time to reflect on how best you can enhance your own benefits package and your family's financial plans. There are many parts of the program, such as the 403(b) and 457 supplemental retirement savings plans that are modifiable during the plan year at any time and for any reason. Furthermore, there are many options available to you outside of the *Choices* Benefits Program that you might wish to consider for the enhancement of you and your family's financial stability and future. This article will explore these various "internal" and "external" options still available to you for the coming year and review the many complex factors you may wish to consider in your attempts to enhance and supplement your own individual benefits program.

I. Enhancing Retirement Benefits – Many parents think that their highest priority should be saving for their children's college educations. While this is an important and a noble goal, most financial planners agree that this should not be the first place that you put your savings dollars. When children reach college age, they have many ways to pay for their education - scholarships, grants, loans, summer or part-time employment, etc. When their parents reach retirements age without adequate savings, their options are fewer and far less attractive - deferring retirement, working part-time after retirement to supplement inadequate income, reducing expenses and sacrificing life-style and travel plans, dropping supplemental health insurance and long term disability insurance and praying that you do not become sick or disabled, etc. When your children are young, their needs seem to take precedence and your own retirement seems so far off that it is easy to forget about it. Nonetheless, enhancing you and your spouse's retirement benefits should be your family's highest financial priority. Otherwise, you run the risk of forcing your children to take care of you in your golden years.

As we have said often in the *Choices Newsletter*, your regular retirement plan and Social Security are only two legs of your three-legged retirement stool. These two legs are usually not sufficient to take care of your long term needs in retirement. Those close to the benefits program see evidence of this all the time. There are many retirees now who must take out their checkbooks to pay for their medical insurance because their TRS or PERS benefit is no longer sufficient to cover cost of the premi-

um. It is not uncommon for a retired couple's medical premium to take up 40 to 50 % of their total Social Security benefit. And saddest of all, many of our former colleagues have been forced to drop our medical plan completely because they can no longer afford the ever-increasing premiums. These long term former members must now live only with Medicare, Social Security, and their very modest TRS or PERS benefits.

Do not let this happen to you. The earlier you start saving for your retirement and the sooner you take steps to enhance your retirement benefits, the easier it will be in the long term and the better the outcome. There are a number of different actions and programs available for this enhancement - IRAs, 403(b) and 457 supplemental savings accounts, prior service purchases, retirement account management and rebalancing, and termination pay management. We will take up each of these programs and strategies in turn.

Supplemental Savings - There are three different programs you can use to build that third leg of your retirement stool - each defined differently by the IRS regulations - IRA plans, 403(b) plans and 457 plans. The last two are even named by the corresponding IRS codes. The IRAs come in three versions: deductible IRAs, non-deductible IRAs, and Roth IRAs. The income restrictions on deductible IRAs are severe (the phaseout begins at \$45,000 per individual and \$65,000 per couple) and many of us would fail to qualify for full deductibility. Non-deductible IRAs are never a good first option, and unless the IRA is fully deductible,

(Continued on Page 2)

choices

The Newsletter of the Montana University System's Flexible Benefits Program

The Choices Newsletter

is designed to help

promote a sense

of our ownership

and responsibilities

within the program.

a deductible IRA should not be your first choice either. While the contributions to a Roth IRA must be made with after-tax dollars, for most people this is nonetheless the best first step, especially for those a long way from retirement. You pay taxes on the contributions as they go in, but you never pay taxes again on the principal nor on the accruals. You can basically take the money out tax-free after age 59 1/2 no matter how much it has grown. Roth IRAs have some real advantages in estate planning, as well, and in transferring funds to your children and grandchildren with minimal tax consequences.

The bottom line - put your first \$3,000 (\$3,500 if age 50 or above) of retirement savings in a Roth IRA in 2004. The maximums for 2005 are \$4,000 and \$4,500 respectively. In most cases both the employee and their spouse can make these contributions. Note that there are some restrictions in income for contributing to a Roth IRA (the phaseout begins at \$95,000 for an individual and \$150,000 for a couple) but since they are quite high, they should not restrict most of us. IRAs are not part of the *Choices* program and cannot be paid for through payroll deductions, so choose your vendor and investment funds very carefully. With all of these various IRAs the tax provisions are quite complex and you would be wise to check with a tax consultant before taking action.

Tax Deferred Annuities - The 403(b) and 457 savings plans allow you to put pre-tax dollars into a retirement account. These plans reduce your taxable income in the years that you contribute, but they are not tax-free. You must pay taxes on these contributions and accruals as regular income upon withdrawal. As with the IRAs, if you withdraw funds prematurely before age 59 1/2, you pay an additional 10% penalty. The beauty of these tax deferred programs is that they effectively give you some 35 to 40% more to invest (the typical amount most people pay in Federal and State taxes) and the money is allowed to grow completely free of taxes until your golden years.

After Roth IRAs, these qualified tax deferred plans are clearly your next best options for retirement savings. The contribution levels are quite generous. MUS employees are allowed to tax defer a total of \$13,000 in 2004 and \$14,000 in 2005 to **both** a 403(b) plan and the 457 plan. The catch-up provisions for those age 50 and above allow for maximums of \$16,000 in 2004 and \$18,000 in 2005. If you participate fully in both, you could set aside \$26,000 to \$32,000 this year alone. Assuming that most of us need some of our salary to live on, few of us ever come close to

reaching these maximums. Yet it is important to realize that it is possible to tax defer these generous amounts in those years where we might receive an unexpected windfall.

Both the 403(b) and the 457 plans are "qualified" by the IRS, and as such, are eligible for payroll deductions. You can sign a tax deferral agreement at any time during the plan year and alter it at any time and for any reason. Six vendors service the 403(b) program: Aetna, MetLife, Scudder, T. Rowe Price, TIAA-CREF, and Valic. You may choose among any of them. The 457 State Deferred Comp program is administered by the Montana Public Employees Retirement Administration (MPERA). As always with any investment, choose your vendor and your funds with great care. Consider your years to retirement and your tolerance for risk and pay particular attention to a fund's expense ratio, the amount of your money your fund manager withdraws every year to cover its administrative cost. Over the long haul, a S&P 500 index fund with an expense ratio of .5% will greatly outperform a similar fund with an expense ratio of 1.5%, for example. Be especially wary of funds with surrender charges. It is your money and why should you be locked into a poorly performing fund for five years or more. Surrender charges protect the investment company, not you. Incidentally, all of these same strategies and advice apply to IRA investing as well.

There is never an ideal time to begin saving for retirement, so start small and start now. Those first dollars in have longer to grow and the amount you will have at retirement might ultimately surprise you. Invest most of your money in tax deferred accounts. The difference between an amount invested in a tax sheltered account and that same amount invested in an after-tax account often ends up being 100s of thousands of dollars. The power of tax deferred compound interest is truly one of the great forces in the universe.

Regular Retirement Plans - There are many strategies that you can use to enhance and maximize your benefits under one of our regular retirement plans. This is especially true as you approach your last years of service.

A. Defined Benefits Plan Strategies:

1. Purchase Service Credit - If you participate in one of our two defined benefit plans - Teachers Retirement System (TRS) or Public Employees Retirement System (PERS), you would be wise to begin purchasing service credit as soon as you are eligible. Both TRS and PERS allows participants to buy up to

five additional years of qualifying service after you are vested with five years of membership service. Credit for military service is sometimes granted without cost to you. The provisions in each plan are complicated and somewhat different. Read your TRS or PERS manuals and contact the appropriate agency. Since interest accrues after eligibility, the sooner you start, the less expensive it will be. For those in good health and anticipating many years as a retiree, applying for and purchasing all the service credit for which you are eligible is a very wise move.

2. Maximize Your Income the Last Three Years Before Retirement - Since your retirement benefit is based on your highest three consecutive years of MUS income (for most employees, their last three years), do everything possible to maximize your income at that time. Beg for that raise, teach summer school, work on grants, work additional hours for additional comp, etc. You might stumble into retirement exhausted, but bear in mind that you could be living many, many years on that TRS or PERS monthly check.

3. Manage your Termination Pay - Termination pay often ends up a sizable amount of money for a long term employee who have had few health problems over the years. How you manage that anticipated windfall can have huge consequences for you both in the size of your retirement check and in how your termination pay is taxed. If you are in TRS and in reasonably good health, Option I is highly beneficial. In this option, you roll all of your termination pay into your final average salary. Crunch the numbers. Most TRS members will see their benefits check go up significantly, often by 100s of dollars per month. By taking Option I you will see none of the termination money up front; in fact, most members will be out-of-pocket for the cost of the Social Security and Medicare premiums on that money. Nonetheless, this move will pay you huge dividends in the long haul. See the TRS handbook for details. While you're at it, be sure that you file a Irrevocable Election Form for Termination Pay 90 days before your effective date of retirement. This enables you to spread the tax payments for your termination pay over the term of your retirement rather than having to pay all of the taxes in a single year.

Managing your termination pay under PERS is a bit more complicated. If a VEBA account is available to you, some or all of your termination pay can be put into this special account. You can then use the VEBA account to pay for your health insurance

(Continued on Page 3)

Enhancing Your Benefits *(Continued from Page 2)*

premiums without ever paying taxes on the amount. Remember that after retirement, you will be responsible for a 100% of the health care premium. By using a VEBA account and pre-tax dollars, you will be saving about a third of the costs. Setting up these VEBA accounts is very complicated. See your payroll/benefits office for more information.

B. Defined Contribution Plan Strategies:

Our defined contribution programs like our ORP administered by TIAA-CREF and our State DC plan administered by MPERA are in some respects less flexible than the DB plans. There are no end-of-the-career strategies that work to significantly enhance your benefits. In DC plans, paying attention over the long haul get results. This means that you should assess your allocations to the various funds and their performances every year and make adjustments accordingly. Evaluate your asset allocation (the percentages you invest in stocks, bonds, fixed funds, etc.) annually and rebalance if necessary. As you approach retirement, adjust your allocations to reflect your shorter time horizon and decreasing ability to recover from a serious market plunge. Contact your fund managers and develop a withdrawal strategy several months before you retire. You can have great success with a defined contribution plan, but only if you pay careful attention and manage your assets well.

II. Enhancing Your Other Benefits: We all get obsessed with retirement and tend to forget that there are other important concerns in the panoply of benefits. Life insurance and long term care insurance come immediately to mind and wise decisions here are equally important for our future.

Life Insurance - The default \$10,000 or \$20,000 in term insurance is too much for many of our employees and woefully inadequate for others. Let's be tough minded here. If you are single, widowed or divorced with no dependent children and no one depending on your income, you simply do not need life insurance at all. Almost everyone has assets sufficient to cover final costs. What MUS provides is more than enough.

If, on the other hand, you are married with dependent children, your family would be devastated by the loss of your income. In this case, you do not need \$20,000 worth of insurance, but likely \$200,000 worth or even \$500,000. Most experts recommend five times your annual salary as a minimum.

Of course, one size does not fit all and much depends on your family's financial situation, your spouse's work and earning power, the ages of your children, etc. The only way most families can afford such large amounts is through term insurance and this is a good option. There is something to be said for keeping your insurance and savings programs separate. Most families could not afford whole life in the amounts high enough to provide real protection and they would end up under-insured.

There is something to be said for purchasing additional term insurance for you and/or your spouse outside of the *Choices* program. Should either of you develop health problems sometime in the future and should you leave MUS employment as well, your insurance would still remain in place and insurability would not be an issue. Two of our vendors - Metlife and TIAA-CREF offer various forms of term insurance at very attractive rates. You may wish to check with them as well as other vendors.

While we are in the tough-minded mode, let's consider life insurance for your children. This form of insurance is largely unnecessary. In the statistically very unlikely demise of a young child, those final expenses would be trivial compared to the cost of supporting that child into adulthood. Better to take that money and put it in the child's college fund.

Long Term Care Insurance - We leave the most complex financial instrument until last. If you are in your 50s, you may wish to consider long term care insurance for you and your spouse. A serious long term illness at the end of your life could devastate your financial resources and leave little for your spouse and heirs. Those with few resources can rely on Medicaid. The wealthy can cover these expenses on their own. All the rest of us should investigate long term care insurance. The November 2003 issue of *Consumer Reports* contains an excellent article on this form of insurance.

Final Thoughts - There are many ways to enhance the *Choices* program and also many ways to shoot yourself in the foot. Cashing out retirement funds upon leaving MUS employment is the worst "disenhancement" step you can take. You will pay full taxes on your withdrawals in a single tax year and a 10% penalty in addition. More importantly, you will be breaking off one leg of your retirement stool completely. You may find yourself sitting on the cold hard ground during your golden years. Don't cash out. ■

The Director's Chair by Glen Leavitt

Every spring, we go on the road around Montana, visiting campuses and experiment stations, to talk about the plan. We also use these meetings to hear what you, the members, have to say. This year our news was mostly good. We are not changing plan design, and most members will see a small decrease in out-of-pocket costs this next year. While listening to employees and retirees, several issues came up often.

Many asked about the new Medicare law passed by Congress late last year (See our Q & A on p. 4). The pharmacy aspects are obviously important to Medicare eligible retirees, but there are aspects that could affect active members as well. One is the new High Deductible Health Plans (HDHPs) with Health Savings Accounts (HSAs). This provision allows a person with a High Deductible Health Plan to set up a savings account with pre-tax dollars that can be used to pay the deductible and other medical expenses. Unlike our Flexible Spending Accounts, any unused funds could be carried over to the next year. The HSA would also be portable and follow the employee to a new job. The HDHP would have to have at least a \$1,000 individual and \$2,000 family deductible and it must include most pharmacy costs in that deductible. The IUBC discussed this type of plan some this spring, but we just didn't have enough information to recommend one. Now that the federal guidelines are starting to come out, we may be able to offer such a plan next year.

Will the plan ever offer dental coverage for retirees? This is something that the IUBC has considered in the past. An optional dental plan for retirees would probably be very expensive if the costs were passed on. Requiring all retirees to take dental coverage would increase the cost of already expensive insurance even more. We plan to revisit this issue with the most recent data next fall.

Why doesn't the indemnity plan cover general physicals and colonoscopies? Traditionally, indemnity plans have not covered medical screens or preventive medicine of any kind. This has been one of the differentiating features between managed care plans and indemnity plans. However, our indemnity plan has adopted some screening procedures and preventive coverage, e.g., mammograms, Pap smears, prostate exams, and the blood chemistry and occult blood screens given through the wellness programs. It also provides for immunizations. The IUBC has looked at offering screening colonoscopies several times, but has not approved this because of the high costs. ■

Questions & Answers

Q I recently have seen many ads and received many mailings promoting Medicare Drug Discount Cards. I am on Medicare now, but purchase my drugs through the MUS mail order program. Should I be considering one of these cards? R. S., MSU-Bozeman Retiree

A. Like everything else in the complicated world of health care, there is no simple "yes or no" answer, only "that depends." The Medicare Card Program was set up as an interim program to cover the gap between the present and full implementation of the Medicare prescription drug benefit in 2006. This drug benefit will be phased in over the next few years.

Phase I - The Card: Starting now (May 2004), Medicare eligible seniors can purchase a temporary card for about \$30 which will entitle them to a 10% to 25% discount on most prescriptions. Low income seniors will get \$600 a year credited to their cards and pay no fee. These cards may be used for discounted drug purchases from June 1, 2004 until Dec. 31, 2005.

Phase II - The Doughnut Hole: In 2006 the card plan will be discontinued and an indemnity plan will replace it. Seniors who elect the plan will pay a \$420 annual premium plus a \$250 annual deductible. Enrollees will get a 75% discount on prescription drug up to \$2,250 in a given year. The plan effectively ends between \$2,251 to \$5,100 and creates the so-called "doughnut hole." After \$5,100, the plan covers 95% of all drug costs.

Phase III - The Sliding Scale: Starting in 2007,

Part B of Medicare, which covers physicians and outpatient services, will cost more affluent beneficiaries considerably more. Rates will be based on a sliding scale.

Card Purchase or Not -To return to the original question, should you purchase one of these cards? If you qualify for the \$600 credit, the answer is - perhaps. The eligibility requirements are very strict, however: no more than \$12,569 in 2004 income for a single and \$16,862 for a couple. All Social Security and pension benefits must be included. Also you must not be eligible for any other drug coverage. **That would mean that you must drop the Choices plan to get the \$600 credit and remember that if you leave the MUS plan, you can never rejoin later.** Go to www.medicare.gov for complete eligibility requirements. If eligible, enter your ZIP code, prescriptions, and maintenance drugs to help you decide which of the approved cards will offer you the greatest benefits.

For those who fail to qualify for the \$600 credit, these cards are probably not worth it. To be certain, go to the Medicare site, choose a card that applies to your local area and enter your prescriptions and maintenance drugs. Then compare costs with the MUS pharmacy and mail order plans. It would be the rare individual who would do better with one of these cards. For most individuals, the best strategy is to stay put for now and use the mail order program whenever possible. Finally, all members should be reassured that MUS has no intentions of dropping health care coverage for our retirees even when the full Medicare drug plan kicks in. ■

CHOICES NEWSLETTER

JERRY COFFEY, EDITOR
ENGLISH DEPARTMENT, MSU
BOZEMAN, MT 59717-2300
PHONE: (406) 994-5327
E-Mail: choices@english.montana.edu
WEBSITE: www.montana.edu/choices

DIRECTOR OF BENEFITS

GLEN LEAVITT
MONTANA UNIVERSITY SYSTEM
2500 BROADWAY
HELENA, MT 59620-3101
(406) 444-6570

BENEFITS PROVIDERS

PEAK (406) 723-3783
NEW WEST (800) 290-3657
FACULTY STAFF ASSISTANCE PROGRAM
APS (800) 833-3031
BLUE CROSS/BLUE SHIELD - MONTANA
(800) 820-1674
MANAGED CARE (800) 782-3083
PHARMACY PROGRAMS
ECKERD (888) 645-9303
RIDGEMAN (800) 630-3214
UNUM LTD (800) 424-2008
LIFE (800) 445-0402
VSP (800) 877-7195

RETIREMENT SYSTEMS

PUBLIC EMPLOYEES RETIREMENT ADMIN.
(406) 444-3154
TEACHERS RETIREMENT SYSTEM
(406) 444-3134
TIAA-CREF (ORP)
(800) 842-2009

ANNUITIES/DEFERRED COMP

MT DEFERRED COMP (800) 981-2786
AETNA (800) 542-0425
METLIFE (406) 452-7250
SCUDDER (800) 323-6105
T. ROWE PRICE (800) 638-5660
TIAA-CREF (800) 842-2009
VALIC (800) 448-2542

Since each individual and family situation is unique, you should always consult your family physician before taking action on any medical advice given here and you should consult your personal financial advisor before acting on any financial advice in the Newsletter. Consult plan documents for complete information.

NON-PROFIT
ORGANIZATION
U.S. POSTAGE
PAID
PERMIT NO. 105
HELENA, MT 59604

Choices
Benefits Program
Montana University System
2500 Broadway
Helena, MT 59620-3101

