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Retirement Withdrawal Rates

Estate Planning for a Second Marriage

Evaluating College Acceptances

Will I have to pay a penalty tax if I withdraw money from my IRA for a down payment on a house?



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Retirement Withdrawal Rates

During your working years, you've probably set aside funds in retirement accounts such as IRAs, 401(k)s, and other workplace savings plans, as well as in taxable accounts. Your challenge during retirement is to convert those savings into an ongoing income stream that will provide adequate income throughout your retirement years.

Your retirement lifestyle will depend not only on your assets and investment choices, but also on how quickly you draw down your retirement portfolio. The annual percentage that you take out of your portfolio, whether from returns or the principal itself, is known as your withdrawal rate. Figuring out an appropriate initial withdrawal rate is a key issue in retirement planning and presents many challenges.

Why is your withdrawal rate important?

Take out too much too soon, and you might run out of money in your later years. Take out too little, and you might not enjoy your retirement years as much as you could. Your withdrawal rate is especially important in the early years of your retirement, as it will have a lasting impact on how long your savings will last.

Conventional wisdom

So, what withdrawal rate should you expect from your retirement savings? One widely used rule of thumb states that your portfolio should last for your lifetime if you initially withdraw 4% of your balance (based on an asset mix of 50% stocks and 50% intermediate-term Treasury notes), and then continue drawing the same dollar amount each year, adjusted for inflation. However, this rule of thumb has been under increasing scrutiny.

Some experts contend that a higher withdrawal rate (closer to 5%) may be possible in the early, active retirement years if later withdrawals grow more slowly than inflation. Others contend that portfolios can last longer by adding asset classes and freezing the withdrawal amount during years of poor performance. By doing so, they argue, "safe" initial withdrawal rates above 5% might be possible. (Sources: William P. Bengen, "Determining Withdrawal Rates Using Historical Data," *Journal of Financial Planning*,

October 1994; Jonathan Guyton, "Decision Rules and Portfolio Management for Retirees: Is the 'Safe' Initial Withdrawal Rate Too Safe?" *Journal of Financial Planning*, October 2004)

Still other experts suggest that our current environment of lower government bond yields may warrant a lower withdrawal rate, around 3%. (Source: Blanchett, Finke, and Pfau, "Low Bond Yields and Safe Portfolio Withdrawal Rates," *Journal of Wealth Management*, Fall 2013)

Don't forget that these hypotheses were based on historical data about various types of investments, and past results don't guarantee future performance.

Inflation is a major consideration

An initial withdrawal rate of, say, 4% may seem relatively low, particularly if you have a large portfolio. However, if your initial withdrawal rate is too high, it can increase the chance that your portfolio will be exhausted too quickly, because you'll need to withdraw a greater amount of money each year from your portfolio just to keep up with inflation and preserve the same purchasing power over time.

In addition, inflation may have a greater impact on retirees. That's because costs for some services, such as health care and food, have risen more dramatically than the Consumer Price Index (the basic inflation measure) for several years. As these costs may represent a disproportionate share of their budgets, retirees may experience higher inflation costs than younger people, and therefore might need to keep initial withdrawal rates relatively modest.

Your withdrawal rate

There is no standard rule of thumb. Every individual has unique retirement goals and means, and your withdrawal rate needs to be tailored to your particular circumstances. The higher your withdrawal rate, the more you'll have to consider whether it is sustainable over the long term.

All investing involves risk, including the possible loss of principal; there can be no assurance that any investment strategy will be successful.

Estate Planning for a Second Marriage

Giving love another chance:

- About 12% of men and women have married twice
- About 3% of each have married three or more times

Source: U.S. Census Bureau, 2011 (data from 2009, most current data available)



You should consider the counsel of an experienced estate planning professional and your legal and tax advisors before implementing any of these strategies. There are costs and expenses associated with the creation of these legal instruments.

They say that love is lovelier the second time around. But for many individuals, remarriage later in life can create some unique estate planning issues.

If you're anything like the typical person contemplating a second (or third) marriage, you are older, have children, have accumulated property, and have been enjoying a standard of living you would like to maintain. Entering into a new marriage can raise many, perhaps conflicting, concerns such as:

- How can you protect assets you already own?
- How can you provide for children from a previous marriage?
- How do you share assets acquired or inherited after the marriage equally or fairly?
- How do you ensure your prospective spouse's future financial security?
- How can you avoid family disharmony?

Put your financial cards on the table

Money is a major cause of stress in any marriage, but it can be especially so in a second one. You and your future spouse should discuss and agree on all important financial issues and formulate plans that, hopefully, you both can live with. Full disclosure is important, especially if you are considering a prenuptial or postnuptial agreement.

Protect your assets with a prenuptial or postnuptial agreement

You're probably well aware that life is not a stroll down the primrose path, so while the suggestion of a prenup or postnup may not fan the flames of romance, you should know that this contract is important if you're bringing assets into the marriage. Why? By law, a surviving spouse has the right to take an "elective share" of the deceased spouse's estate, regardless of what is in the will. An elective share is typically one-third or one-half of the elective estate. An elective estate can include almost all the decedent's property, even property with beneficiary designations and property held in trust. If your surviving spouse takes his or her elective share, this may result in the unintentional disinheritance of your children or other heirs.

The only way to supersede elective share laws is with a prenup or postnup, in which both parties can waive their rights to the elective share. This way, you can minimize the chance that state law will interfere with your intended estate plans.

Revise your will and other estate planning documents

Remarriage does not revoke a will (although state law can trump a will, as we have just discussed). It is vital, therefore, that you draft a new will in light of your new circumstances. While you're at it, review and update other estate planning documents, such as your durable power of attorney, advance medical directives (for example, a living will or health-care proxy), trusts, and beneficiary designations (for life insurance and retirement plans, for example).

Providing for your children from a previous marriage

A big concern in many second marriages is providing for the new spouse without disenfranchising children from a prior marriage. Having your assets pass into a qualified terminable interest property (QTIP) trust can be part of the solution. With a QTIP trust, all trust income is used to support the surviving spouse while the principal is preserved for the children. And there's a bonus: Assets passing to a valid QTIP trust qualify for the marital deduction, helping to minimize potential estate taxes at your death.

Dealing with wealth disparity

In second marriages, it's not uncommon for one spouse to be wealthier than the other. If federal estate taxes are a concern, equalizing your estates so that you and your spouse can take advantage of both of your basic exclusion amounts (\$5,430,000 in 2015) may be in order. Without equalization, you may lose valuable tax savings if the less wealthy spouse dies first. This may be less of a concern now that the applicable exclusion amount is portable. Portability allows a surviving spouse to use the unused applicable exclusion amount of a predeceased spouse. You might also consider state death taxes.

Apportioning estate taxes

If you and your spouse have children from a previous marriage, you may want to plan for the payment of estate taxes in such a way that each child will bear the burden equally.

Conclusion

Each couple entering into a second marriage has unique concerns and goals. It's important to deal with your issues squarely, and create a plan that will optimize dispositions, help minimize taxes, and avoid unintended results, family disharmony, or even litigation.



Evaluating College Acceptances



Comparing costs

To compare colleges based on costs in an apples-to-apples way, determine your out-of-pocket cost, or net price, at each college. Your out-of-pocket cost is the total cost minus any grant or scholarship aid the college is offering. Once you know your out-of-pocket cost at each college, determine how much, if anything, you or your child will need to borrow. Then calculate what the monthly loan repayment amount would be for borrowing amounts at different colleges.

For the majority of high school seniors, spring is crunch time. Most college acceptances arrive in March or April, and a deposit must be received by the college the student plans to attend by May 1. The period of time between acceptances and deposit can be intense as students and their parents weigh a number of factors. Here are two questions to ask as your family evaluates college acceptances.

How well does the college meet your child's needs?

Presumably, all the colleges your child applied to would do a good job of meeting your child's needs; otherwise he or she wouldn't have applied there in the first place. But now that your child has a definite list of options, it's time to look at things a little more closely.

Most colleges host an accepted students day geared exclusively to incoming students. Even if your child has already visited the college, visiting again might be helpful. Your child will meet other accepted students, hear in more detail about the offerings related to academics, extracurricular activities, and student life, and possibly notice things on campus that he or she might have missed the first time around. Some colleges even offer overnight stays in the dorms that can give your child an extra taste of life at that college. Your child might also have the opportunity to explore the surrounding area and see what it would be like to travel back and forth from home. Does the college still have the same appeal that it did when your child applied? If not, why?

If your child can't visit, there are other ways to do additional research. Your child might e-mail a particular department, professor, or student ambassador with specific questions. Your child could also browse online forums for student reviews of specific colleges. While no college is immune from the occasional "sour grapes" reviewer, there might be a ring of truth to a particular issue if more than one student brings it up across multiple forums. At the very least, a cluster of negative reviews might prod your child to investigate further.

Finally, don't overlook academic flexibility. Many college students end up changing their majors down the road. If your child decided to change majors, would he or she be able to find another one relatively easily? Or is the school very focused in one area--for example, business, creative, or technology--where that would be difficult?

What is the cost to you and your child?

Parents of college-bound kids have likely seen the steady stream of news stories about

skyrocketing student loan debt and the debilitating effects of taking on too much debt. For many parents, a thorough review of the affordability of each college is mandatory.

A college acceptance packet should include a detailed breakdown of any financial aid the college is offering, whether it's loans, grants, scholarships (need-based or merit-based), or a work-study job. Make sure to read the fine print carefully and understand *exactly* what the college is offering. For example, a college might say, "Congratulations! You've been awarded \$25,000..." which you might think is a scholarship but which actually includes \$5,500 in loans. As you review the award, keep in mind that if a college says it is meeting "100% of your demonstrated need," the college is the one who defines your need, not you.

The goal is to compare your out-of-pocket cost at each college. To do this, look at the total cost of attendance for each school (this figure includes tuition and fees, room and board, plus a discretionary sum for books, personal expenses, and transportation). Next, list any grants or scholarships the college is offering--this is "free" money. If the grant or scholarship is merit-based, find out whether it's guaranteed for all four years and the requirements that must be met to qualify each year (for example, a 3.5 minimum GPA, participation in certain activities). If the grant or scholarship is need-based, find out whether you can expect a similar amount each year as long as your income and assets stay roughly the same (and you have the same number of children in college), and ask whether it increases each year to match any annual increases in tuition or room and board.

The difference between a college's total cost of attendance and any grant or scholarship aid is your out-of-pocket cost or "net price." Compare your net price across all colleges. Next, with your net price in hand, determine how much, if anything, you or your child will need to borrow. Multiply this figure by four to get an idea of what your total borrowing costs might be over four years. Then use a loan repayment calculator to show your child what the monthly loan repayment would be over a standard 10-year term at a fixed interest rate. Armed with this information, you'll be in a better position to make a sound financial decision for your family.



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Will I have to pay a penalty tax if I withdraw money from my IRA for a down payment on a house?

Whether you may be subject to a penalty tax depends on a number of factors, such as your age at the time of the withdrawal, how quickly you use the funds, and whether the person acquiring the home is a first-time homebuyer.

Distributions from an IRA before you reach the age of 59½ are generally considered premature distributions (or early withdrawals) by the IRS. To discourage withdrawals taken before retirement age, these premature distributions are subject to the usual federal (and possibly state) income taxes in the year received, and the taxable portion may be subject to a 10% federal tax penalty under Internal Revenue Code Section 72(t) (and possibly a state penalty tax). This 10% tax is referred to as the "premature distribution tax."

Fortunately, not all distributions before age 59½ are subject to this penalty. The IRS does allow some exceptions, including one for the payment of first-time homebuyer expenses.

In order for your withdrawal to qualify for this exception, the funds must be used within 120 days to pay the costs of acquiring the principal residence of a first-time home buyer. A first-time homebuyer (you or your spouse, or the child, grandchild, or ancestor of either you or your spouse) is one who neither owned nor had an ownership interest in another principal residence during the two-year period ending on the day the new home is acquired.

Keep in mind that if you qualify for this exception, it is subject to a \$10,000 lifetime limit.



Will I have to pay a penalty tax if I don't have qualifying health insurance?

It depends. One of the main objectives of the health-care reform law, the Patient Protection and Affordable Care Act (ACA), is to encourage uninsured individuals to obtain health-care coverage. As a result of the ACA, everyone must have qualifying health insurance coverage, qualify for an exemption, or pay a penalty tax. This requirement is generally referred to as the individual insurance or individual shared responsibility mandate.

Health insurance plans that meet the requirements of the ACA generally include employer-sponsored health plans, government health plans, and health insurance purchased through state-based or federal health insurance exchange marketplaces.

Individuals who are exempt from the individual insurance mandate include:

- Those who qualify for religious exemptions
- Certain noncitizens
- Incarcerated individuals
- Members of federally recognized American Indian tribes

- Those who qualify for a hardship exemption
- Individuals may also qualify for an exemption if:
- They are uninsured for less than three months
 - The lowest-priced insurance coverage available to them would cost more than 8% of their income
 - They are not required to file an income tax return because their income is below a specified threshold

For tax year 2014, the penalty tax equals the greater of 1% of the amount of your household income that exceeds a specific amount (generally, the standard deduction plus personal exemption amounts you're entitled to for the year) or \$95 per uninsured adult (half that for uninsured family members under age 18), with a maximum household penalty of \$285. In 2015, the percentage rate increases to 2%, the dollar amount per uninsured adult increases to \$325, and the maximum household penalty increases to \$975.



Return on College Investment

Let's say you're giving your niece or grandson some advice on which major to select in college. Do you tell them to get an art degree, or take courses in social sciences? Or should they focus on business and finance?

The decision should not ignore their natural abilities and interests, of course. But if they're looking for the best return on their tuition dollar, then they might consider spending their time in the computer sciences and math buildings.

This information comes from a report published by PayScale.com, which helps people manage their careers and figure out what they're worth on the job market. PayScale's research team tracked the median salary for people who completed its salary survey online. They then compared the 20-year earnings of people following different careers with what was earned, on average, by competing workers with a high school diploma but no college degree. Then they subtracted the cost of 4 years of college tuition, to arrive at a return on investment figure—the additional money the degree provided. Advanced degrees like law and medicine were excluded; the survey focused on bachelors degrees.

The results were striking. Business and finance majors came away with a respectable \$331,345 average ROI over 20 years, but they actually finished a distant third on the list, just ahead of sales, marketing and public relations (\$318,212). The highest ranking majors, by this metric, were computer and math, whose degree-holders saw a net return on their tuition investment of \$584,339 over the 20 years after graduation. These nerdy individuals nosed out the architecture and engineering graduates, whose average ROI came to \$561,475.

Life, physical and social sciences majors fared somewhat less well, earning almost exactly \$250,000 more than their high school diploma competition. Graduates with an arts, design, entertainment and related degree came in last in the survey; they are expected to make a little over \$125,000 as a result of their college training.

Interestingly, the PayScale website also tracks the average return on tuition investment for different colleges. Graduates of Harvey Mudd College in Claremont, CA can expect to earn nearly \$1 million over the 20 years after graduation, with a typical starting salary north of \$75,000—with a 4-year college investment of \$237,700. Numbers 2-10 on the rankings include the California Institute of Technology (\$901,400 earnings, \$221,600 cost); The Stevens Institute of Technology in Hoboken, NJ (\$841,000; \$232,000), the Colorado School of Mines in Golden, CO (\$831,000; \$112,000); Babson College in Wellesley, MA (\$812,800; \$230,200); Stanford University (\$809,000; \$233,300); the Massachusetts Institute of Technology (\$798,500; \$224,500); Georgia Institute of Technology (\$796,300; \$86,700); Princeton University (\$795,700; \$217,300); and the Virginia Military Institute (\$767,300; \$95,700).

You can look up your own alma mater here: <http://www.payscale.com/college-roi/>



Index Changes

Most people think of the major stock indexes as a stand-in for a certain sector or category. The S&P 500 represents large companies, the Russell 2000 tells you what small company stocks are doing, and the Dow represents broad economic sectors. You see tables showing the return of these indices over decades of time, and you might assume that they are made up of the same stocks during that entire time period, instead of trading in and out of stocks like a mutual fund.

But in fact, all of these indices are somewhat actively-managed, in the sense that they move stocks in and out of the index on a regular basis. This became news when the Dow Jones Industrial Average decided to add the biggest company in the world—Apple—to its mix of 30 stocks, replacing AT&T. The Dow has changed slowly but regularly over time; of the 12 stocks in the index when it was announced in 1907, only General Electric remains on the list. Only four companies remain from the 1935 list: GE, DuPont, ExxonMobil and Procter & Gamble.

Sometimes these changes are dictated by the structure of the index itself. Microsoft and Apple were once small company stocks appropriate for the Russell 2000. They have long since graduated out of small company status.

Other times, the index is adjusted to more closely represent the overall economy. The S&P 500 famously added tech stocks in the late 1990s in an effort to catch the fever of the times. In fact, many people might be surprised to discover how much the index changes each year. Looking at the 500 stocks in the current S&P 500 list, you find that 159 firms were not included in the 1970 version. More recently, the index seems to be trading stocks in and out at a faster clip, swapping in 10 stocks in 2010¹, 8 in 2011², 20 in 2012³, 13 in 2013⁴, and 11 in 2014⁵. So far in 2015, the index has dropped Safeway and Covidien, and added HCA Holdings, as well as Endo International.

Since 2010, some notable names were dropped: The New York Times Company, Tribune Co, Office Depot, Eastman Kodak, Qwest Communications, Bethlehem Steel, Owens-Illinois, Novell, Radio Shack, National Semiconductor, Janus Capital Group, Sara Lee Corp, Sears Holding Corp., H. J. Heinz, Sprint Nextel, Advanced Micro Devices, J.C. Penney, Abercrombie & Fitch, U.S. Steel Corp., and Safeway, Inc.

How will substituting Apple for AT&T affect the Dow? Since the Dow is weighted according to the share price of each stock, we can expect movements in Apple stock to greatly affect how the Dow performs going forward. When Visa International undergoes its anticipated four-for-one stock split, Apple's \$100 shares will become the biggest component of the Dow, and a \$10 drop or rise could lead to a 100-point movement in the overall index. A \$33 stock like AT&T would have been far less likely to rise or fall by that dollar amount.

Bigger picture, when you look at the long-term performance of an index, remember that this is not achieved with the same mix of stocks throughout that history. The indices may "trade" more slowly than most mutual funds, but they're turning over their portfolios over time as well.



Lower Oil; Less Looking

You already know that oil prices are lower than they have been in a long time, in part because U.S. oil production is higher than it has ever been, and still climbing steeply. But you have to wonder how long these conditions will last, since lower oil prices make it less economical for oilfield services companies to drill.

The accompanying chart, courtesy of the oilfield services company Baker Hughes, may be the most dramatic illustration of economic reality you will see this month. It shows how the U.S. has increased the millions of barrels of oil per day that we're pumping out of U.S. soil in the past four years. Looking at the orange line rising ever-more-steeply, you wonder whether oil prices will ever go back up to previous levels.

But then you see the purple line, which tracks the number of active oil rigs that are out there looking for new sources of oil. The last quarter of 2014 and the first few months of this year have created a dramatic bear market for drilling rigs in action. In just two fiscal quarters, the number of rigs in the field has dropped almost by half, and there is no sign that the trend is slowing down.

What does that mean? Nothing in the short term, since the orange line represents existing production. But longer-term, you have to expect that fewer active rigs will mean fewer wells and, at the very least, a leveling out of that orange line. Oil prices may be down today, but that doesn't mean supplies will outrun demand forever. Enjoy the low gas prices while you can.

Active Oil Rigs vs Oil Production



¹ NRG Energy, Cablevision Systems, F5 Networks, Netflix, Newfield Exploration Co., Tyco International, Ace Limited, QEP Resources, CarMax and Cerner Corp.

² WPX Energy, TripAdvisor, BorgWarner, Perrigo Co., Dollar Tree, AGL Resources, Cooper Industries, Xylem, Inc., TE Connectivity, Ltd., The Mosaic Co., Accenture PLC, Marathon Petroleum, Alpha Natural Resources, Chipotle, Blackrock, Edwards Lifesciences, Covidien Plc., and Joy Global, Inc.

³ AbbVie, ADT Corp., Alexion Pharmaceuticals, Delphi Automotive, Dollar General, Ensco, Garmin, Ltd., Kinder Morgan, Kraft Foods, Lyondell-Basell, Mondelez International, Monster Beverage, Pentair, LTD, PetSmart, Phillips 66, Blackrock, Joy Global, Covidien, Edwards LifeSciences and Seagate Technology

⁴ Allegion, Ametek, Delta Air Lines, General Growth Properties, General Motors, Kansas City Southern, Macerich, Nielsen Holdings, PVH Corp., Regeneron, TransOcean, 21st Century Fox and Vertex Pharmaceuticals

⁵ Affiliated Managers Group, Avago Technologies, Cimarex Energy, Discovery Communications, Level 3 Communications, Mallinckrodt, PLC, Royal Caribbean Cruises, Martin Marietta Materials, United Rentals and Universal Health Services



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Blog Updates for March: Articles of Interest

Education Planning Articles

None this month

Estate Planning Articles

None this month

Financial Advisor Articles

[10 Questions To Ask A Financial Advisor](#)
[What Does Your Financial Advisor Do?](#)

Financial Planning Articles

None this month

Insurance Planning Articles

None this month

Investment Planning Articles

[The Mistakes That Individual Investors Make](#)

Retirement Plan Articles

[How to Cope With a Lousy 401\(k\)](#)
[Obama takes aim at brokers' fees on U.S. retirement accounts](#)

Retirement Planning Articles

[401\(k\) Lump Sums: What You Need to Know](#)
[8 Questions To Ask Before Taking A Pension Lump Sum Offer](#)
[Does The Retirement Buckets Strategy Really Work?](#)
[How To Turn Your Retirement Savings Into Retirement Income](#)

Tax Planning Articles

[How I Was Stung By A Tax Scam And How You Can Avoid One](#)

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