# MCM Special Report

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## David Kudla, CEO

David Kudla is CEO and Chief Investment Strategist of Mainstay Capital Management, LLC, an independent, fee-only, investment advisor with $2 billion under management. He has been ranked by *Barron's* as one of the **"Top 100 Independent Financial Advisors"** in the country for the past seven years. Mainstay is recognized by *Investment News* as a **"Top 30 Financial Planning Firm"** nationwide. David is a Dow Jones *MarketWatch* columnist and a contributing writer for *Forbes*. He is the Executive Editor of FIA Publishing, LLC which publishes *GM/Delphi 401k Investor* and *Ford/Visteon 401k Investor*. David regularly speaks at national conferences, conducts educational seminars, and advises thousands of automotive employees and retirees. His insights into 401(k) plans, the financial markets, and the automotive industry have been sought out by prominent media sources such as *The Wall Street Journal*, Reuters, *Barron's*, *Forbes*, Bloomberg, NBR, CNN, FOX Business, and CNBC. He has earned two postgraduate degrees, including a Masters Degree in Management at Stanford University. He holds three U.S. patents and has a patent pending for Mainstay's proprietary *Waypoint Retirement Planning System*™.

## Pension Lump Sum Payout

In 2012, General Motors (GM) and Ford Motor Company began offering current employees the option to receive their accrued pension benefits in a lump sum payment upon retirement. At the onset of these programs, the companies also offered a special one-time buyout of remaining pension plan benefits for certain current retirees, including those already receiving monthly pension payments.

A trend to offer pension lump sum buyout programs to retirees occurred among many U.S. companies including Motorola, Visteon, Sears, Kimberly-Clark, Lockheed Martin, and JCPenney. In July 2015, the IRS banned companies from making lump sum offers to retirees who are already taking monthly pension payments.

The lump sum payment of pension benefits shifts the investment risk from the employer to the retiree, but also affords the retiree many potential benefits. This Mainstay Capital Management *Special Report* will review some of the potential advantages and disadvantages of the pension lump sum payment option.

### Investment Risk

With a lump sum payment of pension benefits, the investment risk is transferred from the company to the retiree. Therefore, it is incumbent upon the retiree to ensure he or she has an investment plan to grow the lump sum payment amount over time and provide for a realistic and achievable income distribution plan.

While assuming responsibility for investing the lump sum payment has risk, it also provides several advantages. First, the retiree can invest the lump sum amount as he or she sees appropriate for their individual situation. Second, this creates flexibility in how and when income is distributed from the lump sum amount.

### Tax Risk

While the lump sum payment can be taken as a taxable distribution of your pension benefits, the preferable method is a direct rollover into an IRA. This provides for a non-taxable event and tax-deferred growth until distributions are made. One advantage to the lump sum from a tax standpoint versus the traditional option of fixed income payments is that income distributions can be modified over time. That is, in years you don't need or want the taxable income from your pension you can modify or suspend payments from the lump sum IRA or taxable account now under your control (depending on IRA Required Minimum Distribution status). With the traditional fixed monthly payment method, the income keeps coming with tax liability on those monthly payments. The flexibility to modify income payments from your lump sum allows you to optimize income and tax strategy from year to year.

### Mortality Risk

With the traditional fixed monthly pension payments, the payments stop when you or your surviving spouse dies (with survivorship option). Therefore, if this occurs soon after retirement, nowhere near your full potential pension benefit is ever received. With a lump sum payment, your full pension benefits are paid out and become part of your estate. Therefore, no matter what your life span, your full pension benefits are yours to leave to your heirs or other financial legacy per your estate plan.

Longevity and Inflation Risk

Longevity risk usually implies that if you live longer, you may outlive your retirement assets. The advantage to fixed monthly payments of your pension benefits is that you can never outlive your pension benefits. That monthly check keeps coming until your death and then to your surviving spouse (if you opted for a survivorship option). However, there is a "double-edged sword" to longevity risk. With non-COLA (Cost of Living Allowance) pension plans, such as the General Motors and Ford salaried retirement plans, monthly pension payments are not adjusted for inflation. Therefore, the longer you live, the less your fixed monthly payment buys each year. This is the inflation risk, or purchasing power risk, suffered with fixed monthly payments over time. In today's environment of low inflation, this risk might seem trivial. But even with low rates of inflation, purchasing power continues to erode. If we experience higher inflation rates in the future, this risk could be significant. With a lump sum payment, if inflation rises, appropriate investments can be made to keep pace with inflation or even exceed inflation rates, therefore actually increasing the purchasing power of your pension benefits over time.

PBGC Risk

This risk refers to the possibility that the Pension Benefit Guaranty Corporation ("PBGC"), the government agency that insures pension plans, someday assumes control of your pension plan. In this event, monthly pension benefit payouts could be substantially reduced. In the 2012 special offer program, General Motors transferred a portion of their pension obligations to The Prudential Insurance Company of America, eliminating PBGC risk on those particular pensions. Outside of those transferred pensions, current salaried employees, former employees, and retirees of U.S. companies, including GM and Ford, that choose to receive traditional monthly pension benefits will still be subject to PBGC risk.

Conclusion

The decision between the traditional monthly pension benefit payments or a lump sum payment of pension benefits involves many factors that must be carefully considered in light of your individual situation. For assistance in analyzing your situation and which option may be optimal for receiving your pension benefits, contact Mainstay Capital Management toll-free at 1-866-444-6246 or visit us online at www.mainstaycapital.com for more information on this important topic. Our advisors are standing by; ready to help with your questions and to provide analysis so that you can make a well-informed decision concerning your pension benefits.

## Pension Payment Considerations

- Which pension benefit payment option is best for my personal situation?
- What is the present lump sum value of my pension?
- What are my monthly cash flow needs in retirement?
- How are monthly pension payments impacted by inflation?
- What are the tax implications of a lump sum versus monthly pension payments?
- Do I want the ability to take distributions from my pension benefit at my discretion?
- How does the life expectancy of my spouse and I impact this decision?
- How can each pension payment option impact my estate planning and financial legacy?
- How would my overall retirement income plan change with a lump sum pension payment?
- How can a lump sum pension payment improve flexibility in my income and tax planning?
- What changes should I consider in my Ford SSIP or GM RSP, IRA, and Social Security distributions?