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Buying in to a buyout

What to consider before the money is on the table

By Todd Seibt
tseibt@flintjournal.com · 810.766.6315

More and more companies are using buyouts to peel away layers of employees and pare down payrolls.

But not everyone can - or should - take one.

David Kudla of Mainstay Capital Management in Grand Blanc has counseled thousands of General Motors, DaimlerChrysler, Ford, Delphi, and Visteon Corporation employees planning for retirement in seminars and one-on-one as clients. That includes hundreds who have taken or considered buyouts.

Mainstay, which now has more than $500 million in assets under management, manages 401(k), Individual Retirement Accounts and non-retirement accounts for active, retired and bought-out employees. The firm also provides comprehensive retirement planning and financial planning services.

Kudla provides answers to some questions from the Journal about buyout issues.

Q: There seem to be more buyout plans than ever before. Why?

A: As a result of global competition and industry consolidation, many companies are extending early retirement incentives and severance packages to employees in an effort to reduce the size of their work forces and rein in costs.

Last year alone, buyouts were offered to more than 100,000 automotive workers, and more are coming this year. These initiatives may help a company's bottom line, but for employees, there's much to consider before accepting a buyout.

Q: What should an employee consider before accepting an early retirement package?

A: We talk with a number of people who are emotionally ready to retire, but may not be financially ready to retire. Such a major decision requires a careful assessment of financial needs and resources.

While some expenses will decline or disappear upon retirement, typical retirees need at least 75 percent of their pre-retirement income to maintain their current lifestyle. This percentage can turn out to be much higher depending on health care needs and other expenses.

Q: What's the biggest mistake people make - or almost make - in retiring early as the result of a buyout?

A: The biggest mistake would be accepting a buyout without first developing a comprehensive income and investment plan that realistically accounts for retirement risks.

In our educational seminars, we identify and discuss seven key risk factors facing today's retirees. For instance, people are living longer, healthier lives.

It's quite possible, that people retiring in their 50's will spend more time in retirement than they did in the workforce. Although current income sources may cover a retiree's expenses today, inflation, taxes and longevity continue to take their toll.

Therefore, the retiree will need an increasing income stream over time to keep pace with the increased cost of living expenses. A retirement investment plan should balance preserving wealth with growing the purchasing power of assets to ensure the retiree does not outlive his or her retirement savings.

Q: Buyouts seem to be a normal part of American industry these days. How does an employee know whether to take the current offer or wait?

A: First, the employee needs to weigh the value of the incentives being offered against the benefits of continuing to work. While a buyout package may include cash and other incentives, the employee is giving up a regular paycheck.

This means giving up future pay increases, potentially larger pension benefits and the opportunity to continue to contribute to a company savings plan. However, taking advantage of a sure thing now may be preferable to gambling on the prospects for a better offer down the road, especially if the financial health of the company is in question.

Q: Most buyout programs seem to be cookie-cutter type plans, with no give and take on the rules. Can a worker negotiate anything?

A: We have studied a number of buyout programs over the years. Certainly there are special situations where senior executives have negotiated the terms of their severance.

In most broad-based employee buyout programs, however, while there may be a variety of packages to choose from, there is typically little room for negotiation on specific terms of a package.

We have seen some cases where an employee was not initially offered a package in a round of buyouts, but subsequently convinced their employer to offer them one.

David Kudla, 44, of Mainstay Capital Management in Grand Blanc, has advised thousands of workers on buyouts and early retirement. He has some tips for employees who face, or might face, such offers.

Q: Some buyouts include lump sum payments. Any advice on those?

A: In recent automotive industry buyout packages, lump sum payments ranged from $35,000 to as high as $140,000.

These lump sum payments are intended to help compensate the employee for giving up future wages and other benefits, so it is important to make the most of these dollars. Any lump sum payments should become an integral part of the employee's comprehensive retirement income and investment plan.

Q: Anything in particular to look for in a lump sum payment?

A: The tax treatment on the income.

In the recent Ford buyout packages, some employees were able to roll over the lump sum payment into an IRA. Although not a common option, it offered the employee an opportunity to avoid an immediate tax liability on the lump sum payment as well as provide years of tax-deferred growth.

Q: Is there a best single thing people find out after taking a buyout?

A: Yes. Our clients, who entered retirement with a well-defined income and investment plan are now enjoying a financially secure, very satisfying lifestyle — and many don't miss work at all.