Smart Money Moves for Federal Employees

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Why a Chartered Federal Employee Benefits ConsultantSM

Federal government employees are covered are covered by one of two retirement systems: Civil Service Retirement System (CSRS) or Federal Employee Retirement System (FERS). Additionally, the Thrift Savings Plan (TSP) is available and it plays a different role for CSRS participant than FERS employees.

A Chartered Federal Employee Benefits ConsultantSM (ChFEBC) is a financial professional who has been specially trained on the complexities associated with the retirement and other benefits offered to employees of the federal government. A ChFEBC must complete a training course covering federal employee benefit and successfully pass an examination. Additionally, a financial professional with the ChFEBC designation must complete annual re-certification to remain current with any revisions or updates to federal government benefits.

Because benefits offed to federal government employees are unique and different from what's offered in the non-government or private sector, when your financial professional is a Chartered Federal Employee Benefits ConsultantSM, you're working with someone knowledgeable of your retirement and other benefits.

Participate in the TSP (Thrift Savings Plan)

The Thrift Savings Plan is available to CSRS and FERS employees, but only FERS employees receive matching contributions. FERS employees receive an **automatic** contribution of 1% of base pay from the federal government even if they choose not to contribute from their pay. If a FERS employee elects to contribute to the TSP from their pay, they are entitled to dollar-for-dollar matching contributions (You: $1; Agency: $1) up to three percent (3%) of base pay, For each additional percent above 3% of base pay, there is a fifty percent matching contribution up to five percent (5%) of base pay (You: $1; Agency: $0.50).

Contributions you make to the TSP are made on a **pre-tax** basis meaning that the taxes you pay are computed on the amount of income AFTER the contribution the TSP. So while there are no matching contributions above 5% of base pay, each additional contribution, means that you are paying less in income taxes.

With TSP Contribution		Without TSP Contribution
$50,000	**Salary**	$50,000
-$5,000	**TSP Contribution**	-$0
$45,000	**Taxable Income**	$50,000
11,250	**Taxes @ 25%***	$12,500
	Tax Savings of $1,250	

*25% is the marginal tax rate for a single tax filer that earns $50,000.

Once contributions are made to the TSP, the participant determines into what available options their contributions are made among several options within the TSP. Any earnings, profits, or gains are **tax-deferred**, meaning that the participant doesn't pay taxes on those earnings until the funds are withdrawn.

Participate in the Roth TSP (Thrift Savings Plan)

In 2012, the Roth TSP became available to federal government employees for the first time. Non-government workers had been given the opportunity to participate in the Roth 401(k) and Roth 403(b) plans six (6) years earlier, in 2006.

Unlike contributions to the *original* TSP, contributions to the Roth TSP are **after-tax**, meaning that Roth TSP contributions do not reduce your taxable income. With both the original TSP and the Roth TSP, any earnings, profits, or growth are not taxed while in the plan. Earnings, profits, or growth in the original TSP are **tax-deferred**, meaning you pay taxes on them at some point in the future. Earnings, profits, or growth in the Roth TSP are **tax-FREE** when the participant reaches age 59 ½ and the Roth account has been established for five (5) years.

Original TSP	Feature	Roth TSP
YES	Pre-tax contributions	NO
YES	Earnings aren't taxed while in TSP	YES
YES	Eligible for matching contributions	NO
NO	**TAX-FREE WITHDRAWALS**	**YES**

At first glance, a federal employee may decide not to contribute in the Roth TSP because it doesn't reduce their current taxable income. Current taxation is a significant consideration, but shouldn't be the only consideration. A federal employee made conclude that (s)he may be in a lower tax bracket upon retirement, but that isn't always the case. Let's examine the marginal tax rates for select income ranges and filing statuses:

2016 Marginal Tax Rate	Income (Single Filing Status)	Income (Married filing jointly)
15%	$9,276 to $37,650	$18,551 to $75,300
25%	$37,651 to $91,150	$75,301 to $151,900
28%	$91,151 to $190,150	$151,901 to $231,450

Source: www.irs.gov

The next tax bracket below the 28% tax bracket is the 25% bracket – only a 3% drop. To be in a significantly lower tax bracket, a federal employee would have to have a substantial drop in income to go from the 28% tax bracket to the 15% tax bracket.

Conclusion: For most federal employees, and Americans in general, withdrawals from Roth accounts provide the only potential to receive income that is **TAX-FREE** in retirement. You will have to pay taxes on withdrawals from the original TSP at your marginal tax rate. The Roth TSP option is available to CSRS participants and FERS participants. The consideration should not be original TSP **OR** Roth TSP, but original TSP ***AND*** Roth TSP!

Utilize Other Options in the TSP Besides the G Fund

Below is an overview of the fund choices available in the TSP:

G Fund (Government Securities Investment Fund) - comprised of U.S. Treasury (government) securities where the earnings are based upon the interest rate paid on the government bonds in which the fund invest.
F Fund (Fixed Income Index Investment Fund) - comprised of U.S. government, mortgage-backed, and corporate bonds and seeks to track the performance of the Barclay's Capital U.S. Aggregate Bond Index.
C Fund (Common Stock Index Investment Fund) - comprised of the common stocks of the 500 largest U.S. companies and managed to track the performance of the S&P 500 Index.
S Fund (Small Cap Stock Index Fund) - comprised of common stocks of more than 3,100 U.S.-based corporations with the exclusion of the 500 largest companies represented in the S&P 500.
I Fund (International Stock Index Investment Fund) - comprised of the stocks of companies that make up the Morgan Stanley Capital International EAFE Index. Companies generally are headquartered in Europe, Australia, Asia, or the Far East).
L Fund (Lifecycle Funds) - invests in various mixes or combinations of the G, F, C, S, and I Funds available in the TSP. Designed to take into consideration the participant's projected retirement date, assuming that the more years a person has until retirement, there is a greater need for growth of assets, and therefore would have a greater amount invested in the C Fund, S Fund, or I Fund, versus a participant who has fewer years left and typically more conservative, less concerned about growth, and more interested in preservation of capital and interest paid on bonds in the G Fund and F Fund.

Annual Return of TSP Funds

Year	G Fund	F Fund	C Fund	S Fund	I Fund
2006	4.93%	4.40%	15.79%	15.30%	26.32%
2007	4.87%	7.09%	5.54%	5.49%	11.43%
2008	3.75%	5.45%	(36.99%)	(38.32%)	(42.43%)
2009	2.97%	5.99%	26.68%	34.85%	30.04%
2010	2.81%	6.71%	15.06%	29.06%	7.94%
2011	2.45%	7.89%	2.11%	(3.38%)	(11.81%)
2012	1.47%	4.29%	16.07%	18.57%	18.62%
2013	1.89%	(1.68%)	32.45%	38.35%	22.13%
2014	2.31%	6.73%	13.78%	7.80%	(5.27%)
2015	2.04%	0.91%	1.46%	(2.92%)	(0.51%)
10 Yr Compound Average	**2.94%**	**4.74%**	**7.36%**	**8.03%**	**3.20%**
Growth of $100,000 at the 10-Yr. Compound Average	$133,611	$158,901	$203,435	$216,493	$137,024

Source: www.tsp.gov

For FERS employees, the TSP is designed to make up for the overall less generous annuity benefit payments of the FERS annuity versus the more generous CSRS annuity. The TSP will supplement the FERS annuity and Social Security benefits that a FERS employee would receive in retirement. While employed, a FERS employee should seek to have a greater overall TSP balance because this balance will ultimately determine how much total income a FERS employee will receive in retirement.

In the table below we have taken the example of the growth amounts of $100,000 at the 10-Yr. compound average in the previous table and computed the annual and monthly withdrawal rates for each of the TSP funds.

	G Fund	F Fund	C Fund	S Fund	I Fund
Yearly withdrawal amount at 4%	$5,344	$6,356	$8,137	$8,660	$5,481
Monthly withdrawal amount at 4%	$445	$530	$678	$722	$457

Conclusion: While the G Fund is the safest option in the TSP, it provides the least amount of growth potential. With interest rates at historical lows for U.S. Treasury securities, the growth of your TSP balance will be determined by these interest rates. A Chartered Federal Employee Benefits Consultant℠ can help you determine an appropriate mix of the TSP investment choices to help meet your retirement goals.

Create an Emergency Fund

Life happens. This includes unforeseen car repairs, home repairs, job loss, medical or dental expenses. An emergency fund is important because it serves as a source of funds for life's unexpected occurrences. Those without an emergency fund tend to use the loan feature of the TSP to cover these expenses. This is not an ideal situation because of the opportunity cost or the missed opportunity of having those funds invested. As recently as 2014, the C Fund within the TSP had a 13.78% return for the full year. Someone that borrowed $10,000 from their TSP missed out on their $10,000 increasing in value by $1,378 for that year. Not only is there the missed opportunity of the $10,000 for potential growth, there also the missed opportunity of the $1,378 for any potential growth.

An emergency fund can be combined with a traditional savings account. This account would serve as a "holding account" for any foreseeable and unforeseeable future expense.

A starting point for an emergency fund is to save at least three (3) to six (6) months' worth of living expenses. This would begin to cover any unforeseen events, such as an extended illness or job loss. Any amounts above that level could be used to save for more foreseen expenses such as a family vacation or the expected roof replacement anticipated for the next year.

The takeaway of having an emergency fund is that the TSP at some point will be used to provide you retirement income and the greater the balance, the greater the potential income, to the goal should be to have an emergency fund to cover life's financial setbacks and reserve the TSP for its intended purposed of providing retirement income.

Take Advantage of Favorable Tax Laws

You should know that all income is NOT taxed at the same rate. Depending upon the source, some income can be taxed more favorably (AT A LOWER TAX RATE) than others. From the table below, identify your ordinary income tax rate based upon your income range and filing status

2016 Tax Rates

Ordinary Income Tax Rates	Single	Married, Filing Jointly	Married, Filing Separately	Head of Household
10%	$0 - $9,275	$0 - $18,550	$0 - $9,275	$0 - $13,250
15%	$9,276 - $37,650	$18,551 - $75,300	$9,276 - $37,650	$13,251 - $50,400
25%	$37,651 - $91,150	$75,301 - $151,900	$37,651 - $75,950	$50,401 - $130,150
28%	$91,151 - $190,150	$151,901 - $231,450	$75,951 - $115,725	$130,151 - $210,800
33%	$190,151- $413,350	$231,451 - $413,350	$115,726 - 206,675	$210,801 - $413,350
35%	$413,351 - 415,050	$413,351 - $466,950	$206,676 - $233,475	$413,351 - $441,000
39.6%	$415,051 and up	$466,951 and up	$233,476 and up	$441,001 and up

Source: www.irs.gov

Taxed at Ordinary Income Tax Rates **(10%, 15%, 25%, 28%, 33%, 35% or 39.6%)**	Maximum Tax Rate of 15%*	Maximum Tax Rate of 0%
• Wages • Salaries • CSRS Annuity • FERS Annuity • TSP Distributions • IRA Distributions • Rental Income • Pensions • Interest from CDs • Interest from corporate and government bonds • Short-term capital gains	• Qualified Dividends • Long-Term Capital Gains	• Qualified Roth Account Distributions • Interest from municipal bonds

*If income falls in the39.6% tax bracket, the maximum rate for qualifed dividends and long-term capital gains is 20%.

While you are working, it is important to position your assets so that in retirement you can have income sources from each of the three (3) colored categories above. If your source of income will be a CSRS or FERS annuity and TSP distributions, your income will be taxed as ordinary income at the applicable rates – rates at high as 39.6%. A Chartered Federal Employee Benefit Consultant[SM] can help you position your assets in a manner to take advantage of the difference between ordinary income tax rates and the more favorable rates for qualifed dividends and long-term capital gains (15%) and qualified Roth account distributions and interest from municipal bonds (0%).

Obtain Life Insurance Outside of FEGLI

The Federal Employee Group Life Insurance (FEGLI) provides a Basic Insurance, Option A (Standard Optional Insurance) Option B (Additional Optional Insurance), and Option C (Family Optional Insurance).

The Basic Insurance Amount (BIA) is an employee's annual rate of pay, rounded up to the nearest $1,000, plus $2,000. An employee pays 2/3 of the cost and the federal government pays 1/3. For U.S. Postal employees, the U.S. Postal Service pays the entire cost of Basic Insurance for it employees. The monthly premium amount for all employees, regardless of age, is $0.325 monthly per $1,000 of coverage. For example, someone who earns $53,250 annually would pay $17.31 per month ($0.325 x 53.25), regardless of age, but would have $56,000 in Basic Insurance ($53,250 rounded UP to $54,000 plus $2,000 = $56,000.

Option A, standard optional insurance, is a flat $10,000 of coverage. Unlike, basic insurance, the monthly premium **does** depend upon age and as a federal employee ages (s)he pays more.

Option A Monthly Premiums

Age Group	Monthly	Age Group	Monthly
Under 35	$0.43	**50–54**	$2.38
35–39	$0.65	**55–59**	$4.33
40–44	$0.87	**60+**	$13.00
45–49	$1.52		

Source: https://www.opm.gov/healthcare-insurance/life-insurance/program-information/#url=Premiums-for-Employees.

Option B Monthly Premiums

Age Group	Monthly, per $1,000	Age Group	Monthly, per $1,000
Under 35	$0.043	**60–64**	$0.953
35–39	$0.065	**65–69**	$1.170
40–44	$0.087	**70–74**	$2.080
45–49	$0.152	**75–79**	$3.900
50–54	$0.238	**80 and over**	$5.720
55–59	$0.433		

Source: https://www.opm.gov/healthcare-insurance/life-insurance/program-information/#url=Premiums-for-Employees

It is important for federal employees to obtain life insurance outside of FEGLI because of the prices increases as a federal employee ages, the price of insurance increases by TEN times for an employee who is age 35 or younger ($10.75 per month for $250,000) compared to the monthly premiums when they're age 55-59 ($108.25 per month for $250,000).

It's important to obtain insurance coverage at younger ages when premiums are less and when you are generally healthier at younger ages.

Be Aware of Life Insurance Elections at Retirement

Please know that elections made on the Form SF 2818 Continuation of Life Insurance Coverage (As an Annuitant or Compensationer) are **FINAL** and cannot be changed once filed with the Office of Personnel Management.

On the Form SF 2818, the first election is whether to continue the Basic Life Insurance coverage under the Federal Employees' Group Life Insurance (FEGLI) Program. The next election is at what level you want the FEGLI coverage to continue.

Please see the table below for the most current cost of FEGLI coverage for retirees:

Cost for Annuitants for Each $1,000 of Basic Life Insurance Amount

	75 Percent Reduction	50 Percent Reduction	No Reduction
Until the Month After Your 65th Birthday	$0.3250 monthly	$1.035 monthly	$2.455 monthly
Starting the Month After Your 65th Birthday	Free	$0.71 monthly	$1.94 monthly

Source: https://www.opm.gov/healthcare-insurance/life-insurance/program-information/#url=Premiums-for-Annuitants

The default option for FEGLI is the 75% reduction, resulting in your loved ones potentially receiving less benefits than you planned.

Contact

Have Additional Question About Your Federal Government Benefits?

Call or email today to schedule a no-cost, complimentary phone or in-person consultation:

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Disclosures

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