DaVinci Financial Designs℠

A Financial Life By Design℠

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Happy New Year!

We hope you find the information in this newsletter valuable. Please feel free to call us if you have any questions or concerns. We look forward to speaking to you soon.

Jim, Brad, Stan, Carolyn, Ashley and Jessica.

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The Impact of Health-Care Costs on Social Security

For many retirees and their families, Social Security provides a dependable source of income. In fact, for the majority of retirees, Social Security accounts for at least half of their income (Source: Fast Facts & Figures About Social Security, 2013). However, more of that income is being spent on health-related costs each year, leaving less available for other retirement expenses.

The importance of Social Security

Social Security is important because it provides a retirement income you can't outlive. In addition, benefits are available for your spouse based on your benefit amount during your lifetime, and at your death in the form of survivor's benefits. And, these benefits typically are adjusted for inflation (but not always; there was no cost-of-living increase for the years 2010 and 2011). That's why for many people, Social Security is an especially important source of retirement income.

Rising health-care costs

You might assume that when you reach age 65, Medicare will cover most of your health-care costs. But in reality, Medicare pays for only a portion of the cost for most health-care services, leaving a potentially large amount of uninsured medical expenses.

How much you'll ultimately spend on health care generally depends on when you retire, how long you live, your health status, and the cost of medical care in your area. Nevertheless, insurance premiums for Medicare Part B (doctor's visits) and Part D (drug benefit), along with Medigap insurance, could cost hundreds of dollars each month for a married couple. In addition, there are co-pays and deductibles to consider (e.g., after paying the first $147 in Part B expenses per year, you pay 20% of the Medicare-approved amount for services thereafter). Your out-of-pocket yearly costs for medical care, medications, and insurance could easily exceed thousands of dollars.

Medicare's impact on Social Security

Most people age 65 and older receive Medicare. Part A is generally free, but Parts B and D have monthly premiums. The Part B premium generally is deducted from your Social Security check, while Part D has several payment alternatives. In 2013, the premium for Part B was $104.90 per month. The cost for Part D coverage varies, but usually averages between $30 and $60 per month (unless participants qualify for low-income assistance). Part B premiums have increased each year and are expected to continue to do so, while Part D premiums vary by plan, benefits provided, deductibles, and coinsurance amounts. And, if you enroll late for either Part B or D, your cost may be permanently increased.

In addition, Medicare Parts B and D are means tested, meaning that if your income exceeds a predetermined income cap, a surcharge is added to the basic premium. For example, an individual with a modified adjusted gross income between $85,000 and $170,000 may pay an additional 40% for Part B and an additional $11.60 per month for Part D.

Note: *Part C, Medicare Advantage plans, are offered by private companies that contract with Medicare to provide you with all your Part A and Part B benefits, often including drug coverage. While the premiums for these plans are not subtracted from Social Security income, they are increasing annually as well.*

The bottom line

The combination of rising Medicare premiums and out-of-pocket health-care costs can use up more of your fixed income, such as Social Security. As a result, you may need to spend more of your retirement savings than you expected for health-related costs, leaving you unable to afford large, unanticipated expenses. Depending on your circumstances, spending more on health-care costs, including Medicare, may leave you with less available for other everyday expenditures and reduce your nest egg, which can impact the quality of your retirement.

Think Outside the Shoe Box When Organizing Financial Records

If you have questions about how long to keep copies of your federal tax returns and related records, see IRS Publication 17, Your Federal Income Tax. And because states may have different rules, check with your state's tax authority to find out how long to keep state tax returns and records.

If you've ever had trouble finding an important financial document, you know why it's necessary to keep your financial records organized. Less clutter means less stress, and though you'll need to commit a bit of time up front to organize your files, you can save time and money over the long term when you can find what you need when you need it.

What records do you need to keep?

If you keep paperwork because you "might need it someday," your files are likely overflowing with nonessential documents. One key to organizing your financial records is to ask yourself "Why do I need to keep this?" Documents that you should retain are likely to be those that are related to tax returns, legal contracts, insurance claims, and proof of identity. On the other hand, documents that you can easily duplicate elsewhere are good candidates for the shredder. For example, if you bank online and can view or print copies of your monthly statements and cleared checks, you may not need paper copies of the same information.

How long should you keep them?

A good rule of thumb is to keep financial records only as long as necessary. For example, you may want to keep ATM receipts only temporarily, until you've reconciled them with your bank statement. If a document provides legal support and/or is hard to replace, you'll want to keep it for a longer period or even indefinitely.

Records that you may want to keep for a year or less include:

- Bank or credit union statements
- Credit card statements
- Utility bills
- Annual insurance policies

Records that you may want to keep for more than a year include:

- Tax returns and supporting documentation
- Mortgage contracts and supporting documents
- Receipts for home improvements
- Property appraisals
- Annual retirement and investment statements
- Receipts for major purchases

Records that you may want to keep indefinitely include:

- Birth, death, and marriage certificates
- Adoption papers
- Citizenship papers
- Military discharge papers
- Social Security card

Of course, this list is not all-inclusive and these are just broad guidelines; you may have a good reason for keeping some records for a shorter or longer period of time.

Where should you keep them?

Where you should keep your records and documents depends on how easily you want to be able to access them, how long you plan to keep them, and how many records you have. A simple set of labeled folders in a file cabinet works fine for many people, but electronic storage is another option if space is tight.

For example, one easy way to cut down on clutter and still keep everything you need is to store some of your files on your computer. You can save copies of online documents or purchase a scanner that you can use to convert your documents to electronic form. But make sure you keep backup copies on a portable storage drive or hard drive, and make sure that your files are secure.

Another option to consider is cloud storage. Despite its lofty name, cloud storage is simply an online backup service that allows you to upload and store your files over the Internet, giving you easy access to information without the clutter. Information you upload is encrypted for security. If you're interested, look for a company with a reliable reputation that offers automatic backup and good technical support, at a reasonable subscription cost.

Staying organized

Keeping your financial records in order can be even more challenging than organizing them in the first place. One easy way to prevent paperwork from piling up is to remember the phrase "out with the old, in with the new." For example, when you get this year's auto policy, discard last year's. When you get an annual investment statement, discard the monthly or quarterly statements you've been keeping. It's a good idea to do a sweep of your files at least once a year to keep your filing system on track (doing this at the same time each year may be helpful).

But don't just throw your financial paperwork in the trash. To protect sensitive information, invest in a good quality shredder that will destroy any document that contains account numbers, Social Security numbers, or other personal information.

Whatever system you choose, keep it simple. You'll be much more likely to keep your records organized if your system is easy to follow.

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Buckets of Money: A Retirement Income Strategy

Even with a bucket strategy, you'll probably also need to determine a sustainable withdrawal rate that lets you know roughly how much of your portfolio you can withdraw each year while preserving its longevity.

Don't forget that all investing involves risk, including the possible loss of some or all of your principal, and there can be no guarantee that any strategy will be successful.

Some retirees are able to live solely on the earnings that their investment portfolios produce, but most also have to figure out how to draw down their principal over time. Even if you've calculated how much you can withdraw from your savings each year, market volatility can present a special challenge when you know you'll need that nest egg to supply income for many years to come.

When you were saving for retirement, you may have pursued an asset allocation strategy that balanced your needs for growth, income, and safety. You can take a similar multi-pronged approach to turning your nest egg into ongoing income. One way to do this is sometimes called the "bucket" strategy. This involves creating multiple pools of money; each pool, or "bucket," is invested depending on when you'll need the money, and may have its own asset allocation.

Buckets for your "bucket list"

When you're retired, your top priority is to make sure you have enough money to pay your bills, including a few unexpected expenses. That's money you need to be able to access easily and reliably, without worrying about whether the money will be there when you need it. Estimate your expenses over the next one to five years and set aside that total amount as your first "bucket." Safety is your priority for this money, so it would generally be invested in extremely conservative investments, such as bank certificates of deposit, Treasury bills, a money market fund, or maybe even a short-term bond fund. You won't earn much if any income on this money, but you're unlikely to suffer much loss, either, and earnings aren't the purpose of your first bucket. Your circumstances will determine the investment mix and the number of years it's designed to supply; for example, some people prefer to set aside only two or three years of living expenses.

This bucket can give you some peace of mind during periods of market volatility, since it might help reduce the need to sell investments at an inopportune time. However, remember that unlike a bank account or Treasury bill, a money market fund is neither insured nor guaranteed by the Federal Deposit Insurance Corp.; a money market attempts to maintain a stable $1 per share price, but there is no guarantee it will always do so. And though a short-term bond fund's value is relatively stable compared to many other funds, it may still fluctuate.

Refilling the bucket

As this first bucket is depleted over time, it must be replenished. This is the purpose of your second bucket, which is designed to produce income that can replace what you take from the first. This bucket has a longer time horizon than your first bucket, which may allow you to take on somewhat more risk in pursuing the potential for higher returns. With interest rates at historic lows, you might need some combination of fixed-income investments, such as intermediate-term bonds or an income annuity, and other instruments that also offer income potential, such as dividend-paying stocks.

With your first bucket, the damage inflation can do is limited, since your time frame is fairly short. However, your second bucket must take inflation into account. It has to be able to replace the money you take out of your first bucket, plus cover any cost increases caused by inflation. To do that, you may need to take on somewhat more risk. The value of this bucket is likely to fluctuate more than that of the first bucket, but since it has a longer time horizon, you may have more flexibility to adjust to any market surprises.

Going back to the well

The primary function of your third bucket is to provide long-term growth that will enable you to keep refilling the first two. The longer you expect to live, the more you need to think about inflation; without a growth component in your portfolio, you may be shortening your nest egg's life span. To fight the long-term effects of inflation, you'll need investments that may see price swings but that offer the most potential to increase the value of your overall portfolio. You'll want this money to grow enough to not only combat inflation but also to increase your portfolio's chances of lasting as long as you need it to. And if you hope to leave an estate for your heirs, this bucket could help you provide it.

How many buckets do I need?

This is only one example of a bucket strategy. You might prefer to have only two buckets--one for living expenses, the other to replenish it--or other buckets to address specific goals. Can you accomplish the same results without designating buckets? Probably. But a bucket approach helps clarify the various needs that your retirement portfolio must fill, and how various specific investments can address them.

Note: *Before investing in a mutual fund, carefully consider its investment objectives, risks, fees, and expenses, which can be found in the prospectus available from the fund. Read it carefully before investing.*

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What can I do to protect my username and password information from computer hackers?

At one time, computer hackers were viewed as a few rogue individuals who mainly worked alone. Today, many hackers are part of highly sophisticated networks that carry out well-organized cyber attacks. Unfortunately, these online security breaches can result in your username and password information being compromised.

Whenever you enter your personal information online, you'll want to make sure that you create a strong password to protect that information. Some tips for creating a strong password include:

- Avoid creating simple passwords that have a connection to your personal identity (e.g., date of birth, address) or that can be found in the dictionary
- Create a password that uses a nonsense word/random alphanumeric combination or an arbitrary, easy to remember phrase with mixed-up character types (e.g., upper/lower case, punctuation)
- Don't use the same password for multiple websites
- Use an online tool that allows you to test the strength of a password

If you have trouble keeping track of all of your password information or if you want an extra level of password protection, you may want to use some type of password management software. There are a variety of password managers on the market. Password managers typically work by using high-level encryption methods to store all of your online usernames and passwords on one secure server, using a single master password.

There are a few things you should consider when choosing a password manager. First, if you plan on needing your password information for use on various devices (e.g., tablet, smartphone), you will want to choose a password manager that has mobility features. In addition, some password managers offer added benefits such as web form fillers, which can come in handy if you do a lot of online shopping. Other features to look for include automatic log in and password generator capability.

Do I need to make any changes to my Medicare coverage for next year?

If you're currently enrolled in Medicare, you've probably begun receiving information about your coverage. That's because the annual enrollment period for Medicare runs from October 15 through December 7. During this period, you can make changes to your Medicare coverage that will be effective on January 1, 2014. If you're satisfied with your current coverage you don't need to make changes, but you should review your options before you decide to stay with your current plan.

Your Medicare plan sends you two important documents every year that you should review. The first, called the Evidence of Coverage, gives you information about what your plan covers, and its cost. The second, called the Annual Notice of Change, lists changes to your plan for the upcoming year (these will take effect in January). You can use these documents to evaluate your current plan and decide if you need different coverage. If you haven't already gotten one, you should soon receive a copy of Medicare & You 2013, the official government Medicare handbook. It contains detailed information about Medicare that should help you decide if your current plan is right for you.

As you review your coverage, here are a few points to consider:

- Will your current plan cover all the services you need and the health-care providers you need to see next year?
- Does your current plan cost more or less than other options? Consider premiums, deductibles, and other out-of-pocket costs you pay such as co-payments or coinsurance costs; are any of these costs changing?
- Do you need to join a Medicare drug plan? When comparing plans, consider the cost of drugs under each plan, and make sure the drugs you take will still be covered next year.
- Does your Medigap plan (if you have one) still meet your needs?

If you have questions about Medicare, you can call 1-800-MEDICARE (1-800-633-4227 or TTY 1-877-486-2048) or visit the Medicare website at www.medicare.gov.