

# Guide to the Military's **BLENDED RETIREMENT SYSTEM**



• Choosing Investments



• How Matching Works

• Defined Benefit Plans

• Defined Contribution Plans



• Lifecycle Funds



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To Our Military Members and Their Families:

On behalf of the Defense Credit Union Council and our member credit unions, we would like to take this opportunity to express our sincere gratitude for your selfless service to our nation. To show our appreciation, we are pleased to provide you with this copy of *Guide to the Military's Blended Retirement System* to help you understand the new Department of Defense Blended Retirement System and how it applies to you.

As a proud partner and charter member of the Department of Defense Financial Readiness Campaign, we felt it essential not simply to describe the Blended Retirement System but to provide insights on fundamental retirement planning as well. We also explain why saving is so important and offer practical information for meeting both your immediate and long-term financial goals. We want you to succeed in building a financially secure future!

While the booklet is designed to be informative and to answer questions you may have about the BRS, we highly recommend that you meet with a Personal Financial Manager on your installation as well as with a certified financial planner to discuss your individual financial goals and concerns. In addition, we suggest you make use of all the resources mentioned in the guide and that you look to these reliable sources to gain timely and actionable information.

We wish you all the best as you plan for your retirement. Once again, thank you for your steadfast commitment and courageous service to our great nation!

Sincerely,

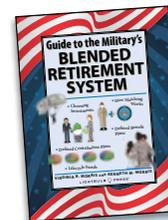
Anthony R. Hernandez  
President and CEO

*Serving Those Who Serve Our Country*

# Guide to the Military's BLENDED RETIREMENT SYSTEM

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# A Retirement Marathon

Ready, set, go on retirement savings.

If you're up for the challenge, you can get a head start on long-term financial security from the minute you join the armed forces. The key is having the discipline to save part of your pay every month—right from the beginning—and for as long as you stay in the service.

Think of retirement savings as a race in which you're competing against yourself. The

goal is to save the money now that you'll need after you stop earning income.

What makes the effort hard, though, is the distance. You're probably wondering why you have to worry now about something that could be 30 or 40 years in the future? There's a simple answer.

*It's the power of compounding.*

## GETTING IN SHAPE

To be competitive in any race, you need to be in great shape physically and mentally. In a retirement savings marathon, it's the mental conditioning that's critical. You have to resist the impulse to buy extra things you'd like to have now to gain something you'll absolutely need later. It's a trade-off that gives you an extra edge, especially down the home stretch.

If you're burdened by debt, saving is almost impossible and you'll find yourself lagging behind. But if the money you're paying in interest on credit cards and loans can go into savings instead, you'll be prepared for the long run.

There's just one good reason to postpone saving for a long-term goal, including retirement. That's using some of your income first to build an emergency fund large enough to cover three to six months worth of living expenses. It's like having disaster insurance for your financial security.

## ON YOUR MARK

All successful competitors have a strategy for reaching their goals and a commitment to seizing every opportunity to get ahead.

For retirement savers, the big opportunity is access to an employer's tax-deferred savings plan that lets you postpone taxes on your earnings. That means your account can compound faster.

There are other routes to the goal, such as a tax-deferred individual retirement account (IRA). But for getting off to a fast start, an employer plan is the way to go.

## HURDLES AHEAD

The perseverance that pushes you to finish a race is like the commitment it takes to be a winner in the retirement marathon. The main difference is that when you're saving for retirement you're apt to encounter hurdles that don't show up on a marathon course, like high inflation and market downturns, which can slow your pace.

But if you plan ahead to deal with them, they won't throw you off your course.

## GET SET, GO

You might hesitate to put money into a retirement savings plan when you're already stretching to cover expenses like supporting a family, buying a home, or keeping up-to-date with your bills.

One approach to paying current costs while saving for the future is to dedicate a percentage of your current income to both short-term and long-term goals. In a perfect world that would be 10% or more, but saving 5% is better than nothing. You can always increase the percentage later on as you're promoted and your income rises.

For short-term savings, you can consider insured accounts, such as certificates of deposit (CDs). Long-term savings, on the other hand, are generally better off in investment accounts that have the potential to grow substantially over time, even if they may sometimes lose value, especially in the short term.

## HITTING YOUR STRIDE

If you start your savings regime early and make a habit of saving during your career, your progress toward accumulating substantial assets should be right on track.

Sooner or later demands on your current income will begin to ease, at least somewhat. The mortgage may be mostly or fully paid off, and your children will strike out on their own. You're likely to be earning more. That means you can gradually contribute a higher percentage to your long-term account through your employer's plan, your own IRA, and other investments you might make.

In fact, the retirement system is set up so that once you turn 50, you qualify to make larger contributions to tax-deferred accounts, whether you spend your entire career in the military or transition to civilian life and participate in a new employer's plan.



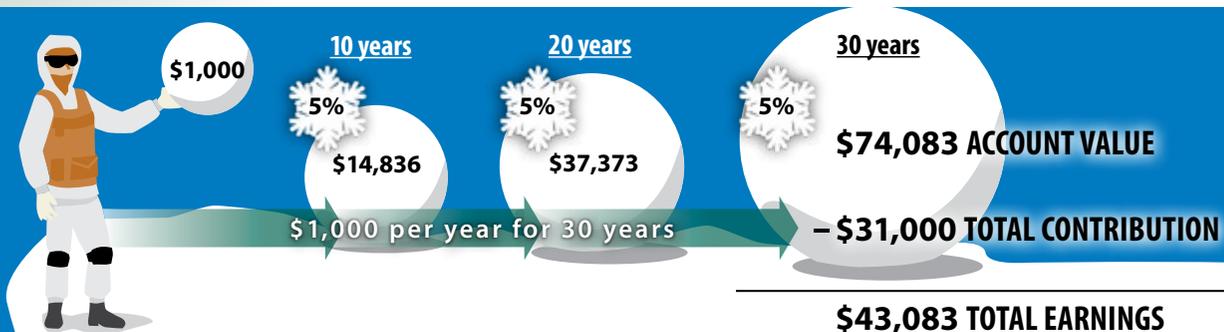
## HOW COMPOUNDING WORKS

As you save, your account balance grows larger when earnings on that money are added to the original amount. That means future earnings are figured on the new, larger base and then added to it, making it larger still.

Compounding is sometimes described as having a snowball effect. If an account

with a balance of \$1,000 gains value at a long-term average rate of 5%, it will be worth about \$1,629 after 10 years, \$2,653 after 20 years, and \$4,322 after 30 years. And if you add \$1,000, or a little over \$83 a month, to the account each year, it will be worth \$14,836 after 10 years, \$37,373 after 20, and \$74,083 after 30. \*

(\* Calculation based on annual growth rate of 5% with annual contribution at beginning of each year.)



# Plan Ahead

Saving should top your must-do list.

## SOURCES OF RETIREMENT INCOME

You've got a fighting chance to make ends meet while you're in the armed forces because you're being paid for the job you do. That's also true if you spend part of your life in a civilian career. But where will your income come from when you're ready to stop working and want to take life a little easier?

### HOW MUCH WILL YOU NEED?

The reason to think about retirement income now is that your cost of living—what you pay for housing, food, clothing, medical care, and all the other things you spend money on—isn't going to be much less after you retire. In fact, you're likely to need at least 80% of your preretirement income, and perhaps as much as 100%, to live comfortably.

For example, someone earning \$50,000 a year will probably need at least \$40,000 a year to maintain the same lifestyle after retirement. And that amount will increase a little every year thanks to inflation, which means that over time your dollars gradually buy less. So you need more income just to keep pace.



## SOCIAL SECURITY

You're entitled to benefits from Social Security because FICA taxes are deducted from your paycheck. The amount you'll receive depends on your earnings in your 35 highest-paid years and how old you are when you start collecting.

While you can count on this income, it's a mistake to think it's all you'll need. The average monthly benefit in 2018 was just over \$1,400—hardly enough to win the retirement marathon.

The other thing to keep in mind is that Social Security is facing a cash crunch of its own. While the government is working to solve the problem, future benefits may be reduced and normal retirement age, which is when you're eligible to receive your full benefit, may be increased. So you have to plan with these possibilities in mind.

When you've collected your final paycheck, you'll ideally be able to tap into some or all of the five primary sources of retirement income.

- Social Security
- Employer-sponsored savings plans
- Individual retirement accounts (IRAs)
- Other individual assets
- Employer pensions

But the amount you can expect from each source depends on your work history and the amount you've saved and invested.

### RULE OF 72

You can use the Rule of 72 to figure out how much inflation will increase your costs. Just divide 72 by the current rate of inflation. The result shows how many years it will take for prices to double. For example, if inflation is averaging 3%, most things will cost twice as much in 24 years.

$$\frac{72}{\text{Inflation Rate}} = \text{Years for Price to Double}$$

## EMPLOYER PENSIONS



Some employers provide lifetime income to employees who have had the required amount of time on the job. For example, members of the armed forces who have 20 years of service collect a pension. But in the civilian world, employer pensions are increasingly rare.

## EMPLOYER SAVINGS PLANS



Like Social Security, employer-sponsored savings plans, including the Thrift Savings Plan (TSP) for members of the armed forces, are a vital source of retirement income. These plans have some major advantages over Social Security. Here's why. The money you contribute to an employer plan doesn't go into a big general account that's used to pay other people's benefits as well as your own. Instead, the money goes into an account in your name, and it's always yours.

What's more, you decide how to invest the money from a menu of choices your plan provides. Since the account grows tax-deferred there's the potential for your balance to grow large enough through compounding to provide a healthy chunk of the retirement income you'll need.

For example, if you accumulated \$500,000 in a tax-deferred account over your working life—not as hard as it may seem if you start early and contribute regularly—you could withdraw 4% in the year you retired to provide \$20,000 in income. The key to lifetime income, though, is that your account would have to continue to grow at a rate as good as or better than the rate at which you withdrew.

To build your account value, and to be able to benefit from this essential income source, you have to agree to be part of the plan, stick with it, and contribute regularly.

## INDIVIDUAL ASSETS



You can create another source of retirement income by opening an IRA, short for individual retirement account. You get the benefit of tax-deferred compounding, just as you do in a TSP account, by contributing a percentage of your earnings. The account is in your name and belongs to you.

People whose employers don't offer retirement savings plans can use an IRA instead. But even those who are part of an employer's plan have the right to contribute to an IRA at the same time, giving their savings a major boost.

You can also accumulate assets, in real estate and other investments, that don't provide tax-deferred compounding but can increase in value over time and be converted to income when you need it in retirement.

### THE WORK OPTION

Before they retire, many people expect to continue to work part-time to make ends meet. But a 2015 survey from the Employee Benefit Research Institute (EBRI) found that while more than two-thirds (67%) of people expect to work after they retire, fewer than a quarter (23%) actually do.

# Employer Plans

Work-based plans are the foundation of long-term financial security.

Employers have the option—though not the obligation—to offer a retirement plan to their employees. These plans generally take one of two forms: a defined benefit (DB) plan or a defined contribution (DC) plan.

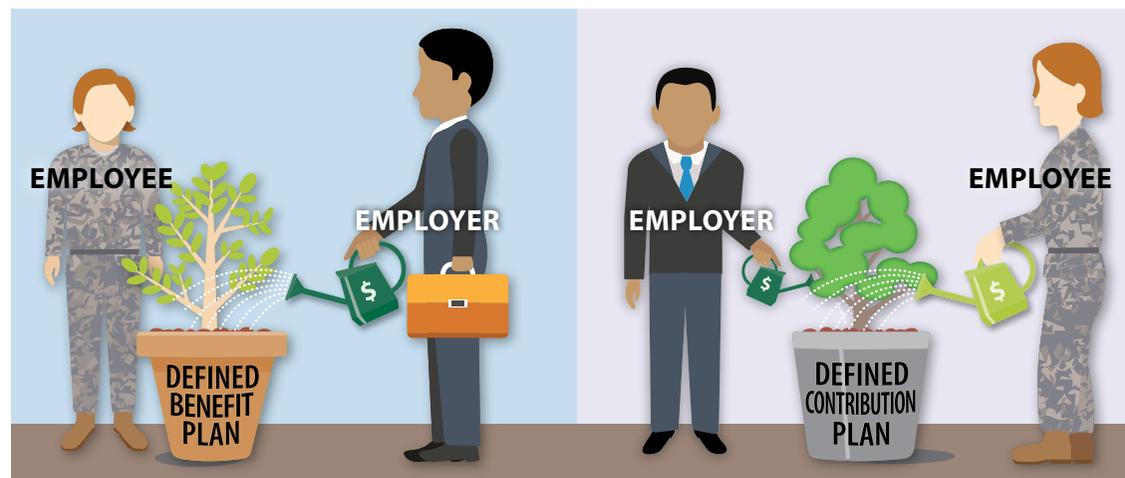
## DEFINED BENEFIT PLANS

A DB plan, commonly known as a pension plan, pays retired employees a lifetime income, usually on a monthly basis. The amount of the pension is typically calculated using a formula that includes the number of years on the job and the employee's final pay, or sometimes the average pay for the most recent three years. As a result, pension income varies, sometimes significantly, from employer to employer, and from employee to employee.

If you have a full-time job with an employer who offers a pension plan, you're automatically

enrolled. Your employer—whether part of the federal government like the DoD, a major corporation, or a nonprofit organization—sets up and manages the plan, invests in a general pension fund that provides income to you and other retired participants, and pays the benefits when they're due.

As a rule, the more you earn and, even more important, the longer you remain in the job, the larger your pension is likely to be.



## AUTOMATIC ENROLLMENT

With some DC plans, it's your responsibility to enroll, decide on the percentage of your pay you'll contribute, and select among the investments offered in the plan. With other DC plans, however, all eligible employees are automatically enrolled, as they are in a DB plan.

Employers who use automatic enrollment choose the initial percentage of pay that participants will contribute to their accounts—often 3% initially—as well as the way the

## DEFINED CONTRIBUTION PLANS

In a DC plan, you, as an employee, are an active participant. Your employer establishes the plan, but it's your responsibility to contribute a percentage of your pay to an account that's been set up in your name within the plan. You're also responsible for spreading your contributions among the investment alternatives the plan offers, a strategy known as asset allocation.

Some employers match your contribution, up to a cap, such as 5% of your base pay. For example, if you contribute 3% of your pay, your employer adds another 3%. If you contribute 5%, your employer adds 5%. So if your plan includes a match, it's smart to contribute at least enough to qualify for the maximum you can receive. Contributing less means you're leaving free money on the table.

Even if you contribute more than 5%, your employer matches only the maximum, or 5%. But that shouldn't stop you from contributing 10% or more if you possibly can. Larger contributions help to build your account more quickly so it can become a substantial financial resource later on.

When you're ready to retire, the value of your account will determine the amount of income you'll have available to withdraw. Unlike a pension, however, the amount isn't guaranteed. Rather, DC retirement income depends on three factors:

- The combined amount you and your employer have contributed to your account
- The return, or what you've earned, on the investments you've chosen
- The number of years your money is invested and can benefit from compounding

## BEING VESTED

When you're vested, you have the right to a pension or to the matching funds your employer has added to your DC account. You earn that right by working at least the minimum length of time required by the plan even if you leave for any reason before you actually retire. But, if you leave before you're vested, you forfeit your rights to the pension or to some or all of the match.



To be vested in the DoD pension plan, you must serve in the armed forces for 20 years. For pension plans offered by corporations and institutions in the private sector, federal ERISA rules require that you are either 100% vested after five years on the job or 20% vested after two years and fully vested after seven years.

The vesting period for an employer's matching contribution varies among DC plans. That's because employers have the right to choose one of three time frames: instant vesting, 100% vesting after three years, or 20% annual vesting starting at the end of the second year, reaching 100% vested after six years.

However, vesting isn't an issue with the money that you contribute to the plan and any earnings on those contributions. They always belong to you, no matter how long you're in the plan.

**C**ost  
**O**f  
**L**iving  
**A**djustment

## HAVE A COLA?

Once a pension is calculated, the base amount is fixed. But government pensions, including those from the DoD, provide an annual cost of living adjustment, or COLA.

A COLA increases the amount you receive and helps combat the effects of inflation that would otherwise erode your buying power. In contrast, corporate pensions, which are much less common than government pensions, rarely include COLAs.

# Blended Retirement System

The DoD has a 21st century retirement package.

The Blended Retirement System (BRS), which launched on January 1, 2018, retains the strengths of a pension-based system while adding a robust defined contribution plan that actively encourages—and also rewards—saving for retirement.

## SAVING, FRONT AND CENTER

With its focus on tax-deferred saving, the blended system modernizes the DoD retirement plan. It also makes the system more equitable by addressing the long-term needs of all service-members, not just those who make the military their career.

To achieve this objective, the DoD has enhanced the role of the Thrift Savings Plan (TSP), making it a key element of retirement planning. Here's a brief summary:

- You'll be part of the blended system, with a TSP account established in your name.
- You'll make contributions to the account from your base pay.
- The DoD will automatically contribute 1% of your monthly base pay to your account starting on your 61st day of service.
- After you've completed two years of service, you'll be eligible for matching contributions from the DoD.

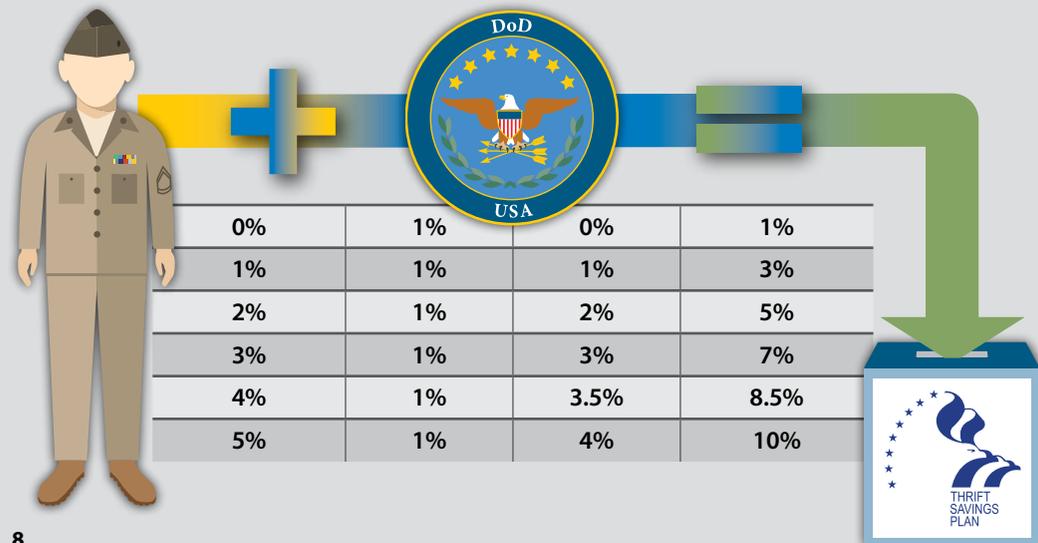
## WHAT'S YOURS IS YOURS

Vesting in your TSP account works differently from vesting in the military's pension system.

Your contributions to your TSP account, plus any earnings those contributions generate, are always yours, regardless of how long you serve.

## HOW MATCHING WORKS

The DoD matches 100% of the first 3% of basic pay that a member contributes to a TSP account, plus 50% of additional contributions, up to 5% of basic pay. That's the same match available to civilian employees in the Federal Employee Retirement System (FERS).



After two years of service, you're fully vested in the automatic 1% contributions that the DoD has made, plus any earnings on those contributions.

At that point, you also begin to qualify for matching contributions. You're immediately vested in the matching amounts the DoD adds to your account and any earnings they produce.

All your vested assets are **portable**, which means you can take them with you when you leave the military. The only amount you risk forfeiting is the 1% the DoD adds to your account during your first two years of service. But that happens only if you leave the military before beginning a third year.

You can move your assets to another tax-deferred account if you don't want to leave them in your TSP account. What you don't want to do is take your TSP savings in cash. If you do, you'll owe income tax plus a potential 10% tax penalty.

## TIME FOR A BONUS

As a way to encourage retention, the DoD will offer a bonus, officially known as career continuation pay, to everyone enrolled in the BRS who stays in the military for at least eight years. The only condition for receiving the bonus is that you must agree to serve a minimum of three additional years. The bonus can be paid in installments to reduce the income tax you might owe if it were paid all at once.

For active duty members, the Secretary of your service branch determines the size of your bonus, which is calculated by multiplying your monthly base pay by a minimum of 2.5, up to a maximum of 13. The Secretary also sets timing of this one-time extra payment, which could be at any point between your eighth and twelfth year of service.

Unsurprisingly, members with the skills the Secretary is most interested in retaining are likely to be offered higher amounts.

Similar incentive payments are available to Reserve members.

## BALANCING GOALS

It always pays to contribute the full 5% of base pay to your TSP account so that you qualify for the full DoD match. The only reason to contribute less is if you're putting money aside to create or replenish an emergency fund as a cushion against unexpected financial problems. For example, you might need this money if your spouse lost a job or your car needed major repairs.

Another resource you can tap into if you're facing a financial challenge is a loan from your TSP account. In the first few years, when your account balance is small, the amount you can borrow may not be enough to meet your need. But as your balance grows, borrowing in this way may be preferable to taking a commercial loan.

TSP loans do have to be paid back with interest. And, while the loan is outstanding, growth in your account is stalled. But as long as the loan is just a temporary interruption, you should be able to get your savings back on track.

## TAKING A LUMP SUM

The blended system will pay retired members a pension annuity in regular monthly installments. But the BRS will also offer members the option of choosing a partial lump-sum payout at retirement.

Members taking a lump sum agree to a reduction in their monthly pension benefit until they turn 67. (That's the age at which you're eligible to collect your full Social Security benefit and so considered full or normal retirement age.) After 67, their full benefit is restored to the amount they would have been paid if they had not taken the lump sum.

## OPTING OUT

You do have the right to opt out of participating in the TSP and not make contributions—but only after you complete financial literacy training. And you will be automatically re-enrolled every year at the default rate. If you're still unwilling to contribute, you'll have to opt out again. You should take the hint. Participate.

# Defined Contribution Plans

These popular plans help kickstart your retirement savings.

Once you're convinced you should start saving now to have the income you'll need in retirement, it's time to take advantage of your employer's retirement savings plan. In your case, as a member of the armed forces, you're eligible for the federal government's Thrift Savings Plan (TSP).

While details of retirement savings plans vary, all offer essentially the same key features: tax-deferral, investment choice, and portability.

## TAX-DEFERRED GROWTH

In all DC plans, the money you and your employer contribute to your account compounds tax deferred. This means no tax is due on your earnings until you begin withdrawing from the account years later. At that point, you pay tax on the withdrawals at the same rate you pay on your other ordinary income.

When taxes are deferred, earnings can accumulate faster since money you would otherwise have to use to pay taxes can keep growing in your account.

The only downside is that earnings in a DC account aren't guaranteed. This means in some years the value of your account may be flat or even shrink. But over the long term, you can expect compounding to help your account grow larger, potentially substantially larger.

## SAVING OR INVESTING?

There's an important distinction between *saving* and *investing*.

**Saving** involves putting some of your current income aside for future use.

**Investing** uses those savings to buy assets that you expect to increase in value, provide income, or both.

In a retirement savings plan, these assets are usually mutual funds that invest in stocks for growth, bonds for income, or a combination of stocks and bonds.

There is, however, a trade-off for tax deferral. With few exceptions, you give up access to your account value until you're at least 59½. If you withdraw earlier, the tax you've deferred is due when you file your tax return for that year. You'll also owe a 10% tax penalty. That's because tax deferral is an incentive to save for retirement. So if you use the money for something else, it will cost you.

There's another concession you make for tax-deferred growth: You must begin withdrawing from your TSP or other DC account when you turn 70½. If you don't, you'll face significant penalties.

## MENU CHOICES

When you're part of a retirement savings plan like TSP, your employer offers a menu of investment choices. This menu lets you choose a combination of investments that put your money to work in different ways. This strategy, called diversification, has the potential to help reduce the risk of losing money or falling victim to inflation while, at the same time, increasing return.

One of the menu choices is designated as the default investment for participants who are automatically enrolled in the plan. Default investments are designed to provide a diversified mix in a single package.

A target date fund, for example, includes a number of different funds under its umbrella. Some of these funds focus on growth and others on providing income. As time goes by and investors in the fund approach retirement, the balance among the funds gradually shifts from an emphasis on growth, which carries higher risk, to an emphasis on reducing risk and generating income.



## TRADITIONAL OR ROTH

All employers that provide retirement savings plans offer traditional tax-deferred accounts. In addition to tax-deferred earnings, you benefit by contributing pretax income, or earnings before income taxes are deducted. This reduces the amount of income that's reported to the IRS and so the income tax you owe. Think of it as a bonus for doing the right thing.

Some employers, including the DoD, also offer a tax-free Roth alternative. If you choose this option, you contribute after-tax dollars, so there's no reduction in your current income tax. But, when you eventually withdraw from a Roth, no income tax is due on the amount you take out, provided you're at least 59½ and your account has been open for five years or more. This means more money in your pocket later on, perhaps more than you would have saved by contributing pretax income.

The only complication in choosing a Roth is that any employer matching funds go into a tax-deferred account that's identically invested rather than into the Roth. You won't accumulate less, but you'll eventually have to convert the tax-deferred account to a Roth or coordinate withdrawals from these accounts.

## PORTABILITY

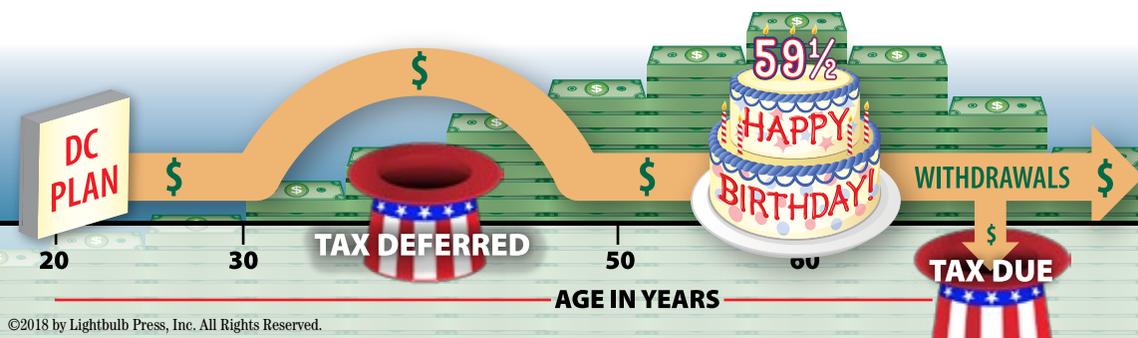
Portability—the ability to take your retirement plan assets with you when you leave the service and take a civilian job—is a major selling point for DC plans.

Portability gives you the flexibility to consolidate your retirement accounts for easier recordkeeping. All you have to do is notify your new employer (if that plan accepts transferred assets) or the trustee of an IRA into which you want to move the assets.

When you authorize a direct transfer from your existing retirement account to a new plan or IRA, the tax-deferred status of the account value remains intact. All you have to do is choose among the investment products available in the new account.

Alternatively, you can stick with your TSP account, since its investment options are hard to beat. Your account will continue to accumulate tax-deferred earnings.

What you don't want to do is cash out. Not only will you owe taxes on the lump sum you receive and the 10% tax penalty. You'll also have to start saving for retirement all over again, beginning with a zero balance.



# Defined Benefit Plans

A pension provides long-term financial security.

If you serve in the active component of the armed forces for 20 years or more, are a member of the Reserve component with the equivalent of 20 years of service, or have a qualifying medical disability, you're eligible for a lifetime government pension when you retire.

The income you receive depends on your **retirement pay base** and your length of service—common factors in calculating a defined benefit pension. In addition, you're entitled to a cost of living adjustment (COLA) in years when rising inflation triggers more than a minimal increase in the Consumer Price Index (CPI).

Unlike civilian pension payments, which typically don't begin before you reach a specific age, such as 65, military pension payments begin as soon as you leave the service. There is an exception, though. Reserve members are generally not eligible to receive their pensions until they turn 60, regardless of the age at which they retire.

## WEIGHING THE ODDS

As valuable as a pension can be, if you're not planning on a military career of at least 20 years,

### IN THE VANGUARD

Military pensions have a long history in the United States. In 1776 the Continental Congress passed a resolution to ensure that those disabled in the fight for independence would receive a pension of half their monthly pay for life or as long as the disability lasted. Over time, the program expanded to cover military widows and orphans, veterans in financial need, and ultimately all those who served for at least 20 years.



you won't be eligible. Currently only 49% of officers and 17% of enlisted men and women reach that milestone.

Job satisfaction is one consideration, both from your perspective and your family's. If you're excited about the next 10 or 15 years of career challenges and opportunities as you rise through the ranks, you might feel confident that you'll have a pension to count on.

But if you see military service as a good transition into a civilian job that really interests you, it's less likely that you'll qualify for the security a pension can provide. That makes it even more critical to contribute as much as you can to your TSP account. Those savings plus retirement savings you accumulate in your civilian life can compensate for not having a pension.

If you anticipate making military service your career, it's probably smart to analyze, to the extent you can, how your branch of the service is likely to evolve over the next decade and how potential changes might affect your career. For example, if there's a continuing trend toward downsizing, how likely are you to face involuntary separation? Are your skills the ones that are likely to be the ones in greatest demand as the force modernizes?



## PENSION CALCULATIONS

The dollar amount, known as the **retirement pay base**, on which a military pension is calculated depends on your base pay and the date you joined the uniformed services.

**Base pay** is what you earn excluding the housing and subsistence allowances that are part of your overall compensation and any additional benefits or special pay.

If you joined the military any time after July 31, 1986, your retirement pay base is determined by your average base pay during the 36 continuous months it was the highest—your **High-3**.

As with most pensions, those with the highest earnings and the longest tenure reap the largest benefit though there is a ceiling, or cap, at the top of the pay scale.

To find your pension in the BRS, your retirement pay base is multiplied by 2% (0.02) for each year of service (YoS).

$$\text{Pay Base} \times (\text{YoS} \times 2\%) = \text{Monthly Pension}$$

### EXAMPLE 1

If your pay base was \$9,000 and you had 25 years of service you'd be entitled to a monthly pension of \$4,500.

$$\$9,000 \times (25 \times 0.02) = \$4,500 \text{ a Month}$$

### EXAMPLE 2

If your pay base was \$6,000 after 22 years of service, your pension would be \$2,640.

$$\$6,000 \times (22 \times 0.02) = \$2,640 \text{ a Month}$$

## JOINING THE RESERVES

Another route to a military pension is combining the years you spend on active duty with enough time in the Regular Reserve component to satisfy the requirement of 20 years of qualifying service.

In that case, the monthly amount to which you're entitled is calculated differently from the formula that involves years of service. But the end result—regular monthly income during retirement—provides similar financial security.

The more time you spend in Active Service, including active duty, active duty for training, and annual training, the more quickly you can accumulate the retirement points you need.

The SBP also provides benefits for minor children and children who are physically or mentally disabled. If you don't have a spouse or children, you may be able to name a SBP beneficiary with an insurable interest—that is, someone who would suffer financially at your death.

There's a monthly premium for SBP protection, which goes into effect at retirement. That amount is determined by the percentage of your pension that your survivors will receive.

## SURVIVOR BENEFITS

Another feature of the military retirement system, the Survivor Benefit Plan (SBP), provides lifetime income, including a COLA, for surviving spouses of retired servicemembers who have served long enough to qualify for a pension.



# Automatic Enrollment

Saving for retirement couldn't be any easier.

When you join the armed forces after January 1, 2018, you'll be automatically enrolled in the Blended Retirement System (BRS). After 60 days—about the length of basic training in most branches—regular contributions will begin to flow into a Thrift Savings Plan (TSP) account that's been established in your name.

Part of the contribution comes from a payroll deduction from your base pay each pay period, and 1% comes automatically from the DoD.

## GETTING AN EARLY START

One of the main benefits of automatic enrollment is that you get an early start on investing for retirement. It would probably be tempting, if it were up to you to enroll, to put off signing up. In fact, planning for something that's not likely to happen for forty or fifty years might seem like a waste of time.

But waiting is a big mistake. That's because the longer you're part of a plan like the TSP, the longer you have to benefit from the power of compounding.

## COMPOUNDING IN TSP

In a bank savings account, compounding occurs when the interest you earn on your principal, or account balance, is added to that principal. The result is a larger base on which future interest is figured. So over time the dollar value of your account increases. Of course, if you take money out, you shrink the principal and slow down the accumulation process.

Compounding works a little differently in an investment fund like those available in the TSP. The contributions you and the DoD make every pay period are used to buy shares in the fund. All the earnings those shares produce are likewise reinvested to buy more shares. So over time the number of shares you own always increases. That's the good news.

But investment accounts are different from savings accounts. If you have \$100 in a savings account, the value of the account is \$100 plus any interest you earn. The value of an investment account, though, depends on two things: the number of shares you own and what each of those shares is worth, as measured by the share price.

What can make you nervous as a new investor is that share prices change. They can and often do go up, but they can also go down before they go back up again. Since you have lots of time before you'll need to withdraw the retirement money in your account, you can ride out those ups and downs. That gives compounding plenty of time to work in your favor.



## EYES ON AUTOMATIC ENROLLMENT

When you're automatically enrolled in a retirement savings plan, your employer chooses the rate at which contributions will be deducted from your pay. That's called the **default rate**. The employer also chooses how your contributions will be invested. That's called the **default investment**. In the BRS, the default rate is 3% of base pay, and the default investment is a TSP lifecycle (L) fund.

For example, if your base pay is \$1,500 a month, or \$750 each pay period at the time you're initially enrolled, you'll contribute \$22.50 ( $\$750 \times 0.03 = \$22.50$ ) twice a month. That's \$540 a year. Then, as you move up in rank over the years, and your pay increases, the amount you contribute will increase as well.

For the first two years you're in the BRS, the DoD contributes an

automatic 1% of your base pay. Using the same \$750 per pay period, the DoD would add \$7.50 ( $\$750 \times 0.01 = \$7.50$ ) twice a month to your account. As you begin your third year of active duty, the DoD will also begin to match your contribution at a rate of 100% of the first 3% of base pay and 50% of additional contributions up to 5% of base pay.

For example, if, at the two-year mark, your base pay has increased to \$1,900 a month, or

\$950 per pay period, and you're still contributing at the 3% rate, you'd be adding \$28.50 twice a month ( $\$950 \times 0.03 = \$28.50$ ) and the DoD will be adding a match of \$28.50 plus the automatic 1% ( $\$950 \times 0.01 = \$9.50$ ). That's a combined total of \$66.50 a pay period or \$1,596 a year.

## CAN YOU SPARE \$28.50?

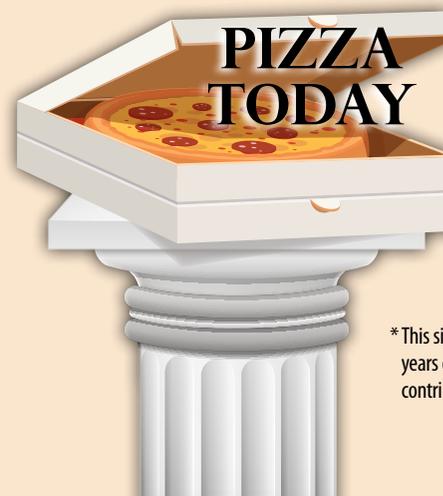
If your first reaction is, "Hey, I need that \$28.50 today not 50 years from now!" you're not the only

one who thinks that way. Retirement is a very long way off and it may be hard to keep up with your bills on what you're earning.

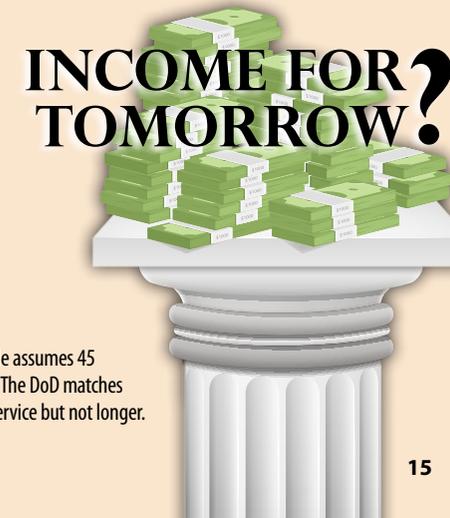
But consider this: If \$1,596 a year was added to your account every year for 45 years, and the earnings compounded at an average annual rate of 6%, you'd have an account worth about \$451,000.\*

And this: If you had used the \$28.50 to buy pizza, you'd have an empty box.

	Base Pay = \$950 per pay period		
	You contribute 3%	DoD contributes 1%	DoD matches 3%
Amount per pay period	$(950 \times .03) = \$28.50$	$(950 \times .01) = \$9.50$	$(950 \times .03) = \$28.50$
Pay periods per year	<u>x 24</u>	<u>x 24</u>	<u>x 24</u>
Annual amount	<u>\$684</u>	<u>\$228</u>	<u>\$684</u>
	\$1,596 contribution per year		
	↓		
	\$451,000 after 45 years at 6%		



OR



\* This simplified hypothetical example assumes 45 years of equal-dollar contributions. The DoD matches contributions through 26 years of service but not longer.

# Spotlight on TSP

You can find the information you need to make smart decisions.

The federal Thrift Savings Plan (TSP) provides access to a user-friendly retirement savings plan for members of the armed forces and other government workers. And the DoD gives you a head start by enrolling you in the plan and setting up an automatic 3% contribution from your earnings each pay period that goes into the default investment, a lifecycle fund.

But it's up to you to explore all the investment options and contribution levels to take full advantage of the plan.

## INVESTING MADE SIMPLE

One of the great benefits of automatic enrollment is that it simplifies decision making. The initial

rate at which you contribute and the way your money is invested are set. Choices like that, especially if you're making them for the first time, can be intimidating. And if you're afraid of making a mistake, you may decide it's easier to do nothing about investing—which is the worst choice you can make.

But it's also good to know that with the BRS, you're not locked in to either the default contribution rate or investment choice. You have the right to contribute at a higher or lower rate. Of course, if you want your account value to grow larger, higher is the way to go. Similarly, if you would rather put your money into the individual funds offered in the TSP, you can make the switch whenever you're ready.

# TRADITIONAL OR ROTH

## CHOOSING A ROTH

One change you might consider right away is having your contributions go into a tax-free Roth account rather than the default tax-deferred account. All you have to do is authorize the change on the TSP website using the automated ThriftLine or by talking to a TSP representative.

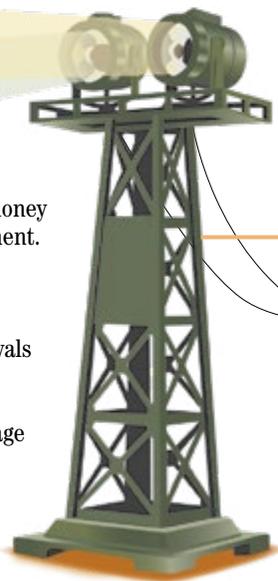
Unlike contributions you make to the default tax-deferred account, those you make to a Roth don't reduce your current taxable income or the income tax you owe.

But the more important difference is what a Roth account will let you do in the future. You'll be able to take totally tax-free withdrawals after you're at least 59½, provided your account has been open at least five years. Chances are your income and your tax rate will be higher than it is now. So tax-free income could mean substan-

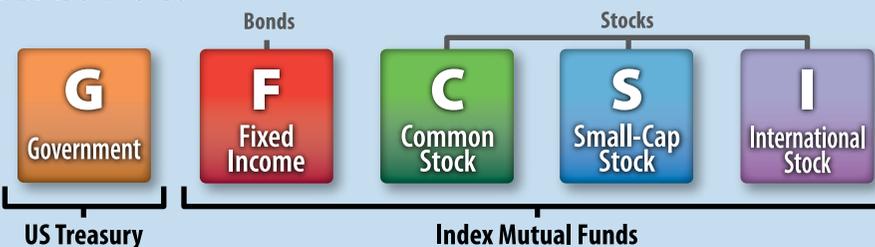
tially lower taxes, and more money in your pocket, during retirement.

And while withdrawals are required from the default tax-deferred account every year after you reach 70½, withdrawals are never required from a Roth account.

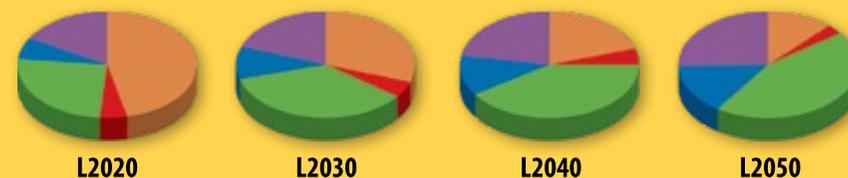
If you want to take advantage of both tax deferred and tax-free withdrawals, you can split your contributions between a traditional and a Roth account any way you choose—for example on a 50-50 or 25-75 basis, or using some other proportion. The only limitation is that the combined total



## INDIVIDUAL FUNDS



## LIFECYCLE FUNDS



## TSP INVESTMENT CHOICES

If you stick with the default investment, your contributions plus the automatic 1% and the matching contributions from DoD you'll qualify for after completing two years of service will go into a lifecycle (L) fund, called the L2050. It's one of a series of L Funds, now including L2020, L2030, and L2040 and eventually L2060.

If you prefer to use one or more of the five individual investment funds (G, F, C, S, and I), the contributions will be allocated to them on the percentage basis you have designated.

The G (for government) Fund invests in a portfolio of US Treasury securities.

you contribute to your accounts cannot exceed the annual cap, or dollar limit, that applies to TSP contributions. That cap is \$18,500 in 2018 and is raised from time to time to reflect increases in inflation.

TSP offers significant flexibility.

You can change the way your contributions are divided between traditional and Roth accounts at any time, stop contributing to either account, or convert your traditional account to a Roth account by paying the taxes that are due. The one thing you can't do is convert a Roth to a traditional account.

## BLENDED RETIREMENT SYSTEM

The other four funds (F for Fixed Income, C for common stock, S for small and mid-sized company stock, and I for international stock) are index mutual funds. An index fund is designed to mirror the performance of a specific stock or bond index by owning all, or a representative sample of, the securities in the index.

The L Funds, which are funds of funds, include all five individual funds in a single package. But each L Fund holds the five funds in different proportions, or weights. For example, the L2050 Fund has 84% of its assets in stock funds, while the L2020 Fund has just 41% in stock funds.

## TAKING AIM AT A TARGET

Lifecycle funds, including the TSP's L Funds, are sometimes described as target date funds. That may provide a clearer sense of what they're designed to do.

Each L Fund is focused on a particular target date that's part of its name and adjusts its portfolio. For example, the L2050 is appropriate for members who won't turn 62 until 2045 or later. In contrast, the L2010 Fund, which reached its target in 2010 and was converted to an income fund, has 74% of its assets in the G Fund to preserve account value for servicemembers invested in this fund and already withdrawing retirement income.

# Investing Basics

Strategic choices help you meet your goals.

If you're new to investing or need a quick refresher before making decisions about your TSP retirement savings account, you might start by thinking about your long-term investment goals.

If you're like many people, it's important to accumulate financial assets that are substantial enough to pay for necessities, such as your living expenses after you stop working, and also let you afford the things that make life satisfying.

The question is, how do you accomplish this objective?

## PRODUCING RESULTS

Achieving the investment result you want depends on several factors. You have direct control over some of the most influential ones, including how much you contribute to your account, how many years you contribute, and which investments you choose.

## RISK AND RETURN

As you make investment choices, it also helps to understand the direct relationship between risk and return. As with other things in life, the more risk you're willing to take, the greater the return it's possible to achieve.



For example, stock and stock funds tend to expose you to more investment risk—meaning the possibility of losing money—than either bonds or cash, primarily because stock prices can be volatile. This means they can change quickly and sometimes dramatically, which bond prices don't tend to do. But stocks and stock funds as a group—though not every individual stock or fund—have a long-term average annual return that's significantly higher than either bonds or cash have produced. That means their value grows at a faster rate than either bonds or cash.

Another type of risk, called inflation risk, is a greater problem with cash equivalent investments and fixed-income investments that pay a low rate of interest. In this case, you don't lose money but your money loses its buying power because your investment earnings don't keep up with inflation, or the regularly increasing cost of goods and services.

## WHY WAIT?

What keeps many people from achieving their financial goals is fear of losing money if they invest. All investments do, in fact, carry some risk.

For one thing, a gain on amounts you invest, which is called your return, isn't guaranteed, as interest on a certificate of deposit (CD) or savings account is. Return can actually be negative in some years.

But you have to balance this possibility against the long-term history of positive results provided by stocks, bonds, and cash equivalents. While it's true that past performance doesn't guarantee future returns, you can be sure that if you don't put your money to work by investing it, it won't grow quickly enough to meet your goals.

## THE AGE FACTOR

When you make investment decisions, your goals are a major factor, but so is your age. The younger you are, and the longer you have until you'll reach retirement age, the more investment risk you may want to take. In your TSP account, this means emphasizing stock funds, specifically the C, S, and I Funds or opting for the L2050 Fund.

- The added risk is offset by the potential to increase your return, which builds the value of your account.
- Equally important, you can afford to take the greater risk because you have a long time to make up for any negative returns, which you're likely to experience from time to time.

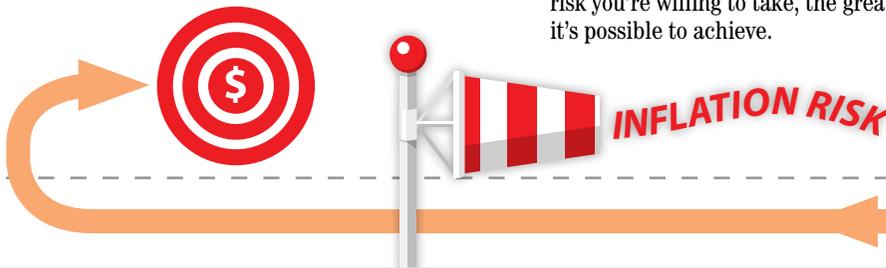
On the other hand, as you grow older, you may want to reduce your exposure to risk and preserve your account value by shifting some assets from more risky to less risky investments. But it's often a good idea to continue to hold stock funds, since the growth they can provide is one way to replenish the amounts you withdraw. It's also a way to help ensure that you don't outlive your money.

## CONTRIBUTION POWER

If you contribute as little as 1% of base pay to your TSP account, you're entitled to contribute up to 100% of any special, incentive, or bonus pay you receive, including all or part of your career continuation pay. There's no DoD match for these contributions, but the cash infusions increase the balance on which earnings can accumulate.

Special rules apply to tax-free combat pay deposited to your TSP account. If the money goes into a tax-deferred account, the contribution will be tax free when you withdraw. But earnings on the contribution are tax deferred, so they'll be taxed as you withdraw them. However, if you deposit the money into a Roth account, both the contribution and earnings on the contribution are tax free at withdrawal.

If you contribute combat pay, though, you'll probably want to consult an experienced tax adviser to ensure that your contributions don't exceed the legal limit and that you report withdrawals correctly when you file your tax return.



## CORE INVESTMENTS

Most investors focus on three categories of investments, called asset classes.

- Stocks and the funds that invest in stocks, described as equity investments
- Bonds and the funds that invest in bonds, described as fixed-income investments
- Cash and cash-like investments, sometimes called cash equivalents

In the TSP, Funds C, S, and I are stock funds, Fund F is a bond fund, and Fund G, which invests in relatively short-term US Treasury securities, in some ways resembles a cash equivalent fund.

You can put your contributions into any or all of the individual funds, divided among them in any proportion you choose. Or, you can stay in the default L Fund for your entire time in the armed forces. The automatic and matching DoD contributions to which you're entitled are invested the same way your own contributions are.



# How Mutual Funds Work

To make smart decisions, you need to understand your choices.

It's possible, even likely, that in the first few months you participate in the BRS you don't spend much time thinking about choosing investments. A 3% contribution from your base pay plus 1% from the DoD will be going into your tax-deferred L Fund. Case closed. And it may stay that way.

But as you learn more about the power of investing to help you meet your long-term goals, you may want to consider the possibility of making future contributions to the individual funds that are available in your TSP account.

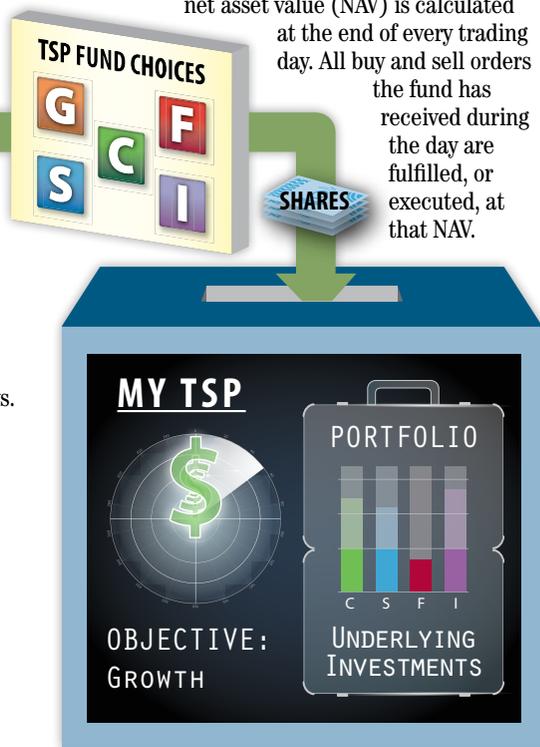
An ideal time to do this may be after your second year of service, when the DoD will begin to match what you contribute. That's also a good time to increase your contribution from the default rate of 3% to 5%. Then you can take full advantage of the DoD match, which will nearly double what goes into your account every pay period.

- TSP Fund F owns bonds issued by corporations, state and local governments, mortgage-backed securities, and the bonds of other countries that have been issued in the United States.

Each fund has an investment objective, which is the goal the fund is designed to achieve. The portfolio is selected to meet the objective. For example, the objective of TSP Funds C and I is growth in investment value.

## BUYING SHARES

Each fund sells its shares to interested investors. Typically, a fund issues as many shares as investors want to buy and buys back any shares investors want to sell. The price per share, called the fund's net asset value (NAV) is calculated at the end of every trading day. All buy and sell orders the fund has received during the day are fulfilled, or executed, at that NAV.



## A MUTUAL FUND OVERVIEW

Like most defined contribution plans, the TSP offers a menu of funds as its investment options. So it's important to understand how these—and other—mutual funds work. That's easier than it sounds since they're basically all alike in several key ways.

Each mutual fund owns a portfolio, or collection, of individual stocks or bonds called its underlying investments. In each case, these underlying investments have some specific features in common. For example:

- TSP Fund C owns stocks of big, well-known companies like Apple and Nike.
- TSP Fund I owns stocks of big companies like Toyota and Nestle with headquarters located in other countries.



## CALCULATION NAV

$$\frac{\text{Value of Investments} - \text{Fees}}{\text{Number of Shares}} = \text{NAV}$$

A fund calculates its NAV by finding the combined current value of all of its underlying investments, subtracting its fees, and then dividing that amount by the number of shares all of its investors own.

As a TSP participant, you accumulate shares in either the L Fund or the funds that you have selected. That happens when the combined contributions from your pay and the DoD is used to buy shares in your name each pay period.

If the combined contribution is enough to buy ten shares of a particular fund, those ten shares are added to your account. This process repeats each pay period, though the actual price of each share can change over time. So, in a hypothetical case, if you bought ten shares in

each of 24 pay periods, at the end of a year your account would have 240 additional shares.

Each fund distributes, or pays out, to its investors the earnings that its portfolio investments generate. This includes either dividends or interest as well as any gains the fund realizes from selling its investments for a profit.

When you own a mutual fund in a retirement account like the TSP, these earnings are always reinvested to buy additional shares. Over time, your share holding can grow substantially.

## PERFORMANCE MEASURES

Good information is essential to good investment decisions both when you make the initial investment and when considering changes in your portfolio later on.

Performance information on TSP funds is readily available on the individual Fund

Information Sheets you can access from the Investment Funds section of the TSP website ([www.tsp.gov](http://www.tsp.gov)).

You'll want to pay attention to the specific risks that each fund carries as well as its recent and long-term performance. Performance is measured in several ways.



**Return on investment (ROI)** measures what you accumulate on the amount you invest, or principal.



**Total return** depends on increase or decrease in value plus any dividends or interest that were reinvested in the fund.



**Percent return** is total return divided by the principal and is the most accurate way to compare the performance of different investments.

The higher the average annual return on your investments, the larger your TSP account balance will be. While it would be nice to be able to expect a return of 15% or 20% a year, that's frankly wishful thinking. But is there a

way to anticipate a reasonable rate of return? Though you should heed the caution that past results don't guarantee future returns, it helps to look at historical returns. They'll give you a sense of what's possible.

# Lifecycle Funds

An L fund provides a turn-key approach to retirement investing.

Each fund that the TSP offers has an investment objective—whether growth, income, or preservation of principal. But no funds are more specific about their objective than the family of lifecycle, or L, funds. Their collective goal is to build and then preserve an account value that will help provide the income that fund investors need for a financially secure retirement.

Each L Fund's **time horizon** is the number of years until the fund's investors plan to begin withdrawing from the fund, usually after they turn 62 but sometimes later. The time horizon largely

determines how the portfolio is allocated—specifically the weights assigned to the five individual TSP funds it holds.

For example, in the L2050 Fund, 84% of the assets are in stock funds (C, S, and I), 12% in the government fund (G), and 4% in the fixed income (F) Fund.

But in the L2020 Fund, with its short time horizon, the emphasis has shifted so that 47% of the assets are in the C, S, and I Funds, 48% in the G Fund, and 5% in the F Fund.\*

\*Allocation targets as of January 2018

## SHIFTING THE FOCUS

An L Fund's portfolio is typically adjusted in a gradual, planned reallocation four times a year, at the end of each quarter. The fund is also rebalanced each business day to ensure its assets are in line with the allocation it intends. Rebalancing occurs in response to changes in market conditions, such as an exceptionally strong stock market performance or an increase in interest rates.

The pace of the reallocation is known as the fund's **glide path** and determines the allocation at the designated, or target, date.

The logic for adjusting the allocation is that a stock-heavy portfolio, even if it is well diversified, as is the case with C, S, and I Funds, tends to be

more volatile than a portfolio with larger allocations to the G and F Funds. Volatility increases the risk of your account losing some of its value, especially in the short term. That becomes less and less appealing as the time you're planning to start withdrawing from your account approaches. That's why L Funds shift their allocations over time away from stocks and into government funds.

But you have to remember that returns on government securities, while not volatile, expose you to inflation risk and the possibility of inadequate income. The longer you live in retirement, the greater this risk becomes.

## BEYOND THE TARGET DATE

When your retirement is years in the future, one question you may not think to ask is what happens when your L Fund reaches its target date. The answer is that it converts to an income fund and keeps your assets invested as you and other fund owners withdraw money over time.

For example, the current TSP Income fund, formerly the L2010 Fund, has 80% of its assets in fixed income and

government securities and 20% in stocks. Even more conservative lifecycle funds eliminate stock holdings entirely at the target date. On the other hand, some more aggressive lifecycle funds maintain substantial stock holdings for 30 years or more beyond the target date, only gradually reducing the allocation to 20%.

It's an important difference, since the way a fund is invested has a major impact on the amount that's likely to be available each year for the rest of your life.

## MAKING SMOOTH MOVES

If you change your mind after investing your assets, you can move money out of an L Fund and into individual TSP funds at any time by making an interfund transfer (IFT) request. The only exception is that after you've made two IFTs in a month, additional transfers in that month must go into the G Fund. However, making multiple changes in quick succession rarely if ever improves the performance of your portfolio.

Transfers work the other way as well. If you allocate your contributions to individual funds when you begin to contribute to your TSP account, you can always move your account balances into an L Fund at any point in your career.

Any transaction fees you incur for an IFT are nominal, unlike the high fees and significant penalties charged by some other retirement investments you may be offered, such as fixed, variable, or index annuities.

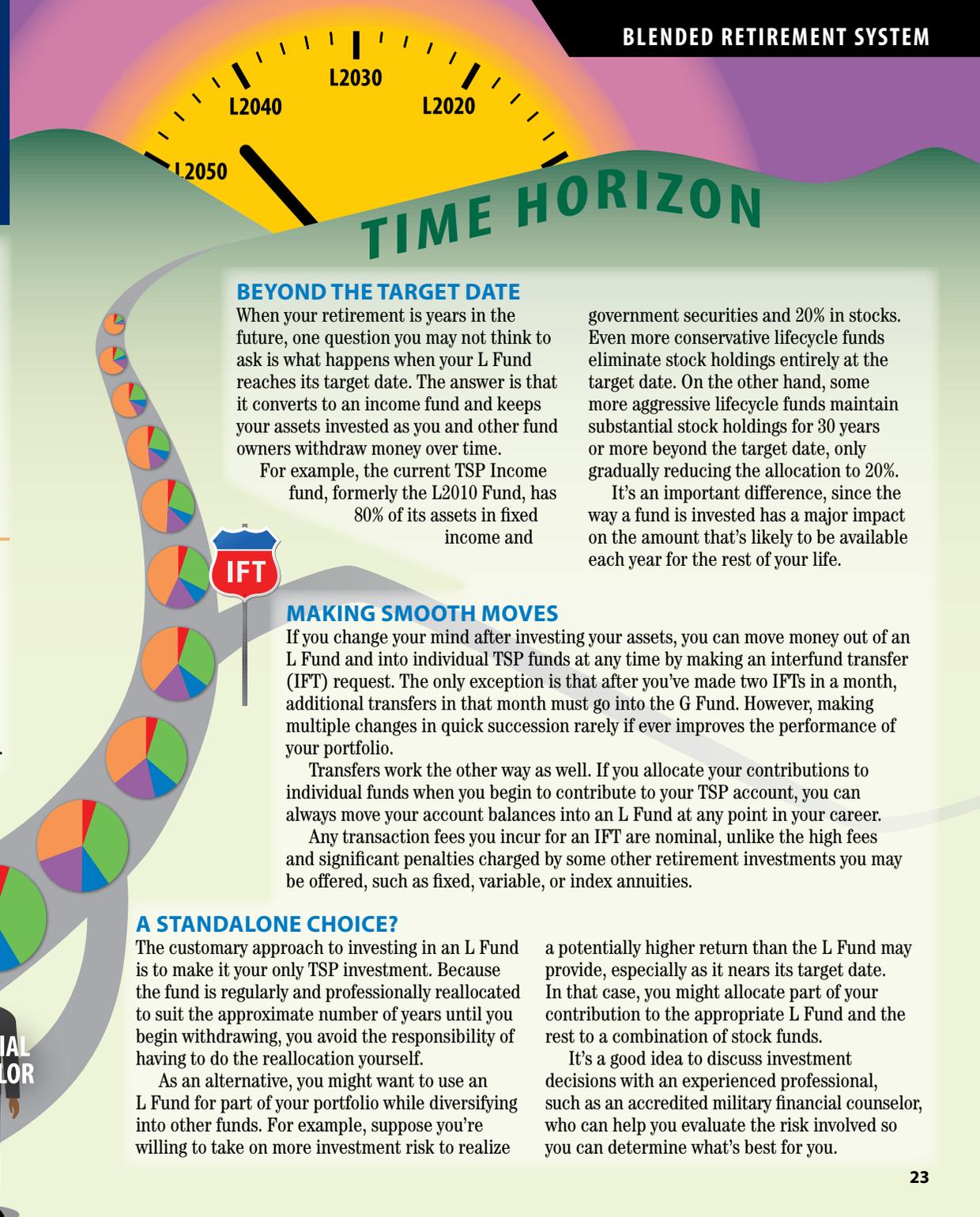
## A STANDALONE CHOICE?

The customary approach to investing in an L Fund is to make it your only TSP investment. Because the fund is regularly and professionally reallocated to suit the approximate number of years until you begin withdrawing, you avoid the responsibility of having to do the reallocation yourself.

As an alternative, you might want to use an L Fund for part of your portfolio while diversifying into other funds. For example, suppose you're willing to take on more investment risk to realize

a potentially higher return than the L Fund may provide, especially as it nears its target date. In that case, you might allocate part of your contribution to the appropriate L Fund and the rest to a combination of stock funds.

It's a good idea to discuss investment decisions with an experienced professional, such as an accredited military financial counselor, who can help you evaluate the risk involved so you can determine what's best for you.



# Investing for Growth

A growing account value requires nurturing.

When you invest for growth, your goal is to increase the value of your account. You want it to be worth more—ideally significantly more—than the amount you and the DoD contribute to it. While there's no guarantee you'll be as successful as you'd like to be, choosing appropriate investments is an essential first step.

What are those investments? When you participate in the TSP, they're the three stock funds—C, S, and I. When you invest outside the TSP, perhaps in an individual retirement account (IRA), they include individual stocks, other stock mutual funds, exchange traded funds (ETFs) that invest in stocks, and real estate investment trusts (REITs) that invest in commercial real estate.

## THE EQUITY ADVANTAGE

When you buy shares of a stock, you have an equity, or ownership, interest in the corporation that issued them. As a part owner, however tiny your share of the company, you stand to benefit if it's profitable. Often, though not always, a profitable company pays out a portion of its gains to shareholders, or owners, as a quarterly dividend.

What's more, the stock prices of a successful company tend to increase over time because investors want to buy shares. Since there is only a limited supply, demand drives the price up. If a stock's price goes up, you can sell your shares for more than you paid for them. That gives you a profit, known as a capital gain.

The alternative to selling is to hold on to your shares as their price goes up. Their growing value provides the increase in account value you were seeking. And if you reinvest all your dividends and capital gains, you'll provide an additional boost to your quest for growth.

Of course, stock prices sometimes go down instead of up, and dividends are sometimes cut. You have to anticipate that. But offsetting this risk is the fact that, over long periods of time,

**GROWTH INVESTMENTS, including stocks, stock mutual funds and ETFs, have the potential to increase in value and build your retirement assets.**



stocks in general, though not every individual stock, have always provided a financial gain.

## INDIRECT OWNERSHIP

You get the same potential benefits by owning stock mutual funds and ETFs as you do by owning stocks. But instead of direct ownership, you own these stocks indirectly. That's because what you actually buy are shares in a fund or ETF that owns a portfolio of individual stocks.

The advantages of using funds and ETFs is that you don't have to make the hard decisions about which stocks to buy, what to pay for them, and when to sell them. Those decisions are made for you.

What's more, there's a great variety of funds. This makes it relatively easy to find funds that match your objectives and your attitude toward investment risk.

In addition, mutual fund and ETF share prices tend to change more slowly than the share price of individual stocks. This reduces volatility risk, or the possibility that a price will drop suddenly, exposing you to a potentially big loss if you were to sell when the price was down.

The reduced risk occurs because each fund owns dozens, or sometimes hundreds or even thousands, of different stocks. While some of the underlying stock prices may change quickly at any time, it's much less likely that all of them will drop at the same time.

## INDEX FUNDS

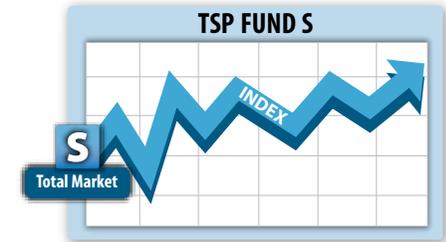
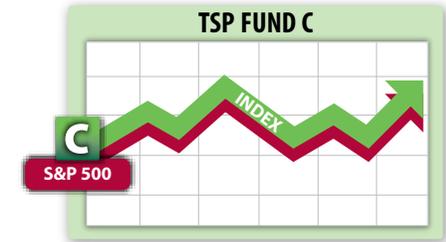
You can take two approaches to building the value of your investment portfolio with stock mutual funds. One is to invest in index funds like the funds offered in the TSP. The other is to invest in actively managed funds.

An index fund portfolio holds the investments that a market index tracks. For example, the TSP Fund C is invested in an index fund linked to the S&P 500 index that owns the 500 large and medium-sized US companies in that index. TSP Fund S is invested in an index fund that tracks the Dow Jones US Completion Total Market. That index includes several thousand mid- and small-company US stocks that aren't included in the S&P 500.

An index fund's objective is to replicate the performance of its underlying index. That's why index investing is also called passive investing. The portfolio is determined by what the index measures, not by an active manager.

## ACTIVELY MANAGED FUNDS

In an actively managed fund, a professional manager chooses the



portfolio based on research findings and a particular investment style. The manager's goal is to outperform, meaning do better than, the return on the relevant market index. For example, if a fund invests in large US companies, the index it wants to beat is the S&P 500.



## IT'S ABOUT FEES

Index funds typically charge investors lower fees than an actively managed fund that makes similar investments. One reason is that an index fund's portfolio changes only when the securities in the underlying index change. That can be as infrequently as once a year. So transaction costs are minimal. Actively managed funds cost more because they tend to trade frequently to meet their objective and because they pay salaries to their managers and research teams.

The bottom line is that the lower a fund's fees, the more of its return goes toward building your account value.

## WHAT'S AN INDEX?

An index is a list of securities that share a distinctive characteristic, such as asset classification, market capitalization, or investment objective, and whose collective performance indicates how a specific segment of an investment market is performing.



# Investing for Income

The ultimate goal of saving for retirement is producing income.



**INCOME INVESTMENTS, such as bonds and CDs, provide interest payments on a regular basis that can be a source of income after retirement.**

One aspect of retiring that makes many people uneasy is whether they'll have enough money to cover their needs and do the things they enjoy. They won't be paid every two weeks or every month. Yet they'll still need to pay their living expenses.

Social Security helps to cover some of those costs, as does a pension if you have one. But the real difference between living comfortably in retirement and struggling to make ends meet is the amount of income you'll have from the investment assets you have accumulated.

That income generally includes the earnings your investments produce each year plus a percentage of the total value of your assets.

## INCOME INVESTMENTS

Most investments that are described as income investments pay interest, typically at a rate that's fixed when the investment is issued, or made available for purchase. For example, corporations sometimes raise money to fund expansion or other projects by issuing bonds for investors to purchase

rather than selling stock. Local, state, and federal governments also raise money by issuing bonds.

To encourage you to buy their bonds, these issuers promise to return your principal—the amount you invested—at the end of the bond's term and pay you interest for the use of your money. It's similar in some ways to buying a certificate of deposit (CD), where you earn interest for the CD's term and then get your money back.

This sounds like a good deal to many investors, especially those who are new to investing or worried about losing money with stocks. Bonds have a fixed value, and though their prices do change during their term, change tends to happen fairly slowly and rarely dramatically.

So why does the TSP L2050 Fund, the default investment for people entering the armed forces now, have only 16% of its assets in interest-paying funds and 84% in stock funds?

## IT'S ALL ABOUT EARNINGS

Compared to equity investments, interest-paying investments have a more limited potential to provide growth in value. Since the price of a stock has the potential to double or more over a period of several years, and many stocks provide dividend income, the return on stocks over time may be substantially greater than the return on most bonds.

If early in your career you put more than a small percentage of your twice-monthly contributions into income funds, especially the G Fund,

you run the very real risk that your earnings won't keep up with inflation. This can undermine your potential to increase your account value.

## HOW BOND FUNDS WORK

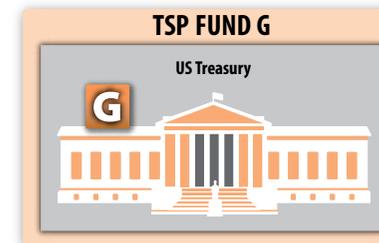
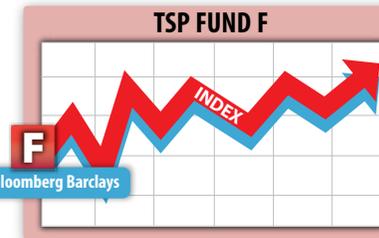
There is an important difference between owning individual bonds and owning a bond fund. With an individual bond, you know the interest rate you're earning and when the bond's term ends. That's called its maturity date, and it's when you get your principal back.

A bond fund, like other mutual funds, holds many different investments—in this case a portfolio of individual bonds, each with its own interest rate and maturity date. So when you buy a bond fund, you're not promised either earnings at a specific rate or return of principal.

Instead, when you buy shares in a bond fund, you receive income distributions from the interest paid by the bonds in the fund's portfolio pay. You also receive your share of any capital gains the fund realizes from selling bonds for more than it paid to buy them.

The fund will buy back any shares you want to sell. You might do that, for example, if you decide to move some assets from your bond fund to a stock fund.

Like stock funds, bond funds can be index funds or actively managed funds. The TSP Fund F is an example of the former. Its assets are held in a separate account that tracks the Bloomberg Barclays US Aggregate Bond Index, and its portfolio changes each time the bonds in the underlying index change. Fund G, though also an



## RED FLAGS

Be very wary of any websites that link information about the BRS to products they want to sell you. They're unlikely to put your best interest ahead of their own profit motive.

income fund, isn't invested in a mutual fund. It owns a portfolio of US Treasury issues.

## NEARING RETIREMENT

When you're within ten or fewer years of leaving the work force for good—which could be up to forty or more years after you've left the armed forces—you'll probably want to move some of the assets in your TSP portfolio from the C, S, and I Funds to the F and G Funds to reduce the risk to your portfolio of a stock market downturn.

Even then you may want to leave some assets in the stock funds for their growth potential. While the G Fund, in particular, protects your principal, it provides very little growth in value. And since there is a very real possibility that you'll live 15 or 20 years after you stop working, it may be smart to continue to invest for some growth for as long as possible.

## COMPARATIVE PERFORMANCE

A Wells Fargo study released in October 2016 compares the portfolio growth of two different investment portfolios over the forty years between January 1, 1976, and September 30, 2016. A \$10,000 portfolio with 70% in stocks and 30% in bonds grew to \$581,295 while one with 30% in stocks and 70% in bonds was worth \$336,715.



# Allocate and Diversify

Successful investing isn't something you can do by the seat of your pants.

If you're serious about meeting your financial goals, you need to make strategic investment decisions.

You can start by allocating your portfolio, which means dividing your principal among different categories of investments, usually on a percentage basis. The core categories, called asset classes, include stocks and stock funds, bonds and bond funds, and cash equivalents. Each asset class shares a set of defining features that distinguishes it from the others. For example,

all stocks and stock funds give you equity in the company issuing the stock.

As a next step, you diversify, or achieve variety, within each asset class. That's important because smaller categories within each broad asset class typically behave differently from each other even though they all share the defining features of that class. For example, all bonds mature after a specific number of years. But bonds with one-year terms are much less vulnerable to inflation than bonds with 30-year terms.



## ALLOCATING ASSETS

Allocation is a strategic move because it positions you to benefit from investment performance while helping to protect you against investment risks.

Here's why. No one asset class consistently provides the strongest return year after year. And different classes tend to produce their strongest returns at different times. That's the result of a number of factors, including what's happening in the markets themselves and in the overall economy. For example, if corporations have strong earnings and increase their dividends, they attract investors. That drives up their stock prices, increasing return. But if earnings falter while interest rates are rising, stock return may decline while bond return rises.

What's more, a class that has been a strong performer for a year or two often turns out to be a weak performer in the next year. While this pattern is predictable, its timing isn't. So it makes sense to own some stocks and some bonds all the time. Then you stand to benefit regardless of which one is performing better.

While allocation positions you to have a profit, it also helps to reduce investment risk. If you have all your money in stocks while stocks are doing well, what will happen in the next phase of the investment cycle when stock prices falter? You could have major losses. But if you always have some money in bonds, the gains in that asset class can help offset periodic losses in stocks.

Remember, though, that there is always a risk with investing. Allocation is a strategy—it doesn't guarantee a profit or protect against losses in a falling market.

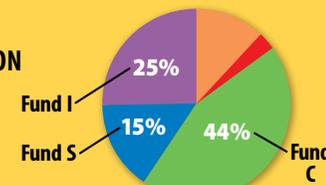
## TURNING THEORY TO PRACTICE

If you're ready to move ahead with your investment strategies, it's smart to take your age into account. The younger you are, the larger the percentage of your total contribution you may be comfortable putting into stock funds, perhaps 80% to 90%. The next step is to divide the total among the three TSP stock funds: large-company US stocks (C), small and medium-sized company US stocks (S), and international (I) stocks.

The ratio you choose is up to you. You might start by using the L2050 Fund as a model: It has 44% of its assets in Fund C, 15% in Fund S, and 25% in Fund I.

That means each pay period, 44% of your contribution and 44% of the DoD contribution will go into Fund C, 15% of each into Fund S, and 25% of each into Fund I. And it's worth repeating that unless there's a compelling financial reason, you'll want to contribute at least 5% of your base

STOCK ALLOCATION IN THE L2050 FUND



pay to qualify for the full match that begins at the start of your third year of service.

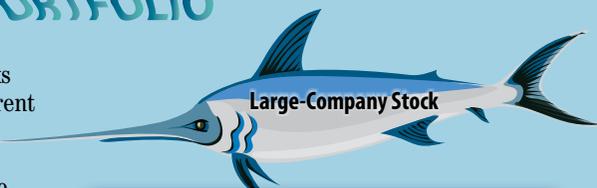
Remember, though, that you're not locked into your choice. You might assign equal percentages to each of the three TSP funds or use some other allocation. As you become a more experienced investor, you can easily change the equity portion of your portfolio as well as your overall allocation. One thing you don't want to do, though, is to try to outsmart, or time, the market by shifting money among your funds based on speculation about what will happen next. That's a losing game.

## DIVERSIFYING A PORTFOLIO

Diversification is another way to help manage risk and improve performance. While all stocks put your money to work in a similar way, different types of stocks respond differently to changes in the stock market and the overall economy. Big companies do better in some periods while small ones do better in others. And stocks in US companies do better some years while stocks in international companies do better in others.

Diversification also helps protect you against problems in an individual company, like poor management decisions or strong competition, which can undermine its performance.

One good way to diversify is to buy mutual funds instead of individual stocks and bonds. Mutual funds give you access to the performance of a broad market or specific market segment by holding portfolios of individual securities. This provides the variety you're looking for in a single package.



## CASTING A WIDER NET

If you're investing outside your TSP account, you might also put some money into real estate, commodities, or other investment products in addition to the three basic classes. Greater variety can both enhance return and increase risk protection.

That's one reason that mutual funds are the most common investment option in retirement savings accounts, including the TSP.

Small-Company Stock



International Stock



# Other Ways to Invest

You're not limited to one way to invest.

A rule of thumb for achieving long-term financial security is to save 10% to 15% of your pretax income. After you've contributed enough to your TSP account to qualify for the full match, you may want to explore other investment opportunities.

At the top of the list is a low-cost individual retirement account (IRA). It's a good way to gain exposure to a broader range of investments than the TSP offers and further diversify your portfolio.

With an IRA you can take advantage of tax-deferral, just as you can with TSP.

In addition, you may want to open a taxable account. Your dividends, interest earnings, and capital gains are taxed in the year they're paid. But the rate at which those taxes are calculated is always lower than the tax rate that applies to your regular income.

## IRAS: DOING IT YOUR WAY

IRAs are personal retirement plans. You choose where to open your account—with a mutual fund company, bank, or brokerage firm—and how to invest your money. The financial institution you choose is the custodian of your account.

The only requirement for being able to contribute each year is that you have earned income, which is money you're paid for work you do. What's important, too, is that you can contribute to an IRA even if you're participating in the TSP or another employer plan at the same time. It doesn't have to be one or the other.

There are two types of IRAs: traditional, tax-deferred IRAs and Roth IRAs. The earnings in both types are tax-deferred, which means you don't have to withdraw money to pay taxes on your earnings. As a result, your full balance can compound and your account value can grow more quickly.

When it comes to withdrawals, however, the two types of IRAs are quite different. With a traditional IRA, you'll eventually have to begin taking money from your account and pay tax on those withdrawals. You can relax though—that doesn't start until you're 70½. That's a lifetime from now.



<b>SIMILAR</b>	Earnings on both types of IRAs are tax-deferred	
<b>DIFFERENT</b>	Must pay taxes on withdrawals	No tax due on withdrawals
	Must begin withdrawals at 70½	Never required to take withdrawals

With a Roth IRA, no tax is ever due on the earnings, even when you take them out, provided you are at least 59½ and your account has been open at least five years. And you're never required to take withdrawals if you don't want to or don't need the money.

## TAKING ADVANTAGE OF AN IRA

An IRA can be a valuable tool for managing your investments.

While you usually can't withdraw from an IRA without penalty before you turn 59½, you can take out money if you need it for certain specific needs. These include buying a first home, paying

## DEDUCTIBLE IRAS

You may qualify to deduct your contribution to a traditional IRA—though not a Roth IRA—and reduce your current income tax. To qualify you must either not be eligible for an employer plan or have a modified adjusted gross income (MAGI) that's less than the limit the government sets for the year.

Of course, while you're in the armed forces you are eligible for an employer plan.

But you may qualify for a deduction based on income. In 2018, those limits are \$63,000, phased out at \$73,000 if you pay taxes as a single filer and \$101,000 to \$121,000 if you're married and file a joint return.

### 2018 INCOME QUALIFICATIONS

Single	\$63,000 - \$73,000
Joint	\$101,000 - \$121,000

## TAXABLE ACCOUNTS

You might wonder why you'd bother with a taxable account when you can take advantage of tax deferral on other accounts. There are several reasons:

1. When you invest in a taxable account, you can invest as much as you are able and choose any investments you prefer, not just those offered by a plan sponsor. This may be an advantage in reaching your goals.
2. Dividends and capital gains are taxed at a lower rate than regular income, while all withdrawals from traditional tax-deferred accounts are taxed at the same rate as your regular income.
3. You can use the money for any goal that's important to you, at any time you need the money.
4. You are never required to take withdrawals from taxable accounts, which gives you more flexibility in managing your retirement income.

## WORD TO THE WISE: REINVESTMENT

If you own mutual funds in a taxable account, you can choose to take the earnings the funds distribute and any capital gains as cash. But at least until you retire, and probably longer, it's always smart to reinvest so you can continue to build your account value.

5. You can make tax-exempt investments, such as municipal bonds, in a taxable account so no taxes are due on the interest they pay. But if you buy these investments in a tax-deferred account you actually owe tax on the interest.

a child's college tuition, or covering medical expenses. You'll owe income taxes, but no penalty. And, if you have a Roth IRA, you can withdraw up to \$10,000 tax free to buy a first home.

You can roll over, or move, money from your TSP account or other employer plan into an IRA when you leave your job for any reason. There are

no penalties, no taxes due, and no loss of tax-deferred status. Like money in an employer plan, up to \$1 million in an IRA is protected against creditors. The same is true of all the money in your TSP account. What this protection means is that you can't be forced to withdraw to pay off any debts except federal tax liens.

# Powering to the Finish

Retirement saving provides the extra kick you need to reach your goal.

You should expect a flurry of financial decision-making when you transition from military life to the civilian world, which could happen in your 20s, 30s, 40s, or 50s.

Whether you resign or retire from your branch of service, you're likely to begin a new job where you can build on the retirement savings you've accumulated in your TSP account.

## MANAGING YOUR ACCOUNT

One of the first decisions you may make is what to do with the balance in your TSP account—though there's usually no need to act quickly. You'll have three options.

**Option 1:** If your balance is at least \$200, you can leave it in the TSP. Your balance will continue to compound, and you can reallocate your account holdings just as you could when you were contributing. And you'll still benefit from being part of an extremely low-cost plan. However, you won't be able to make additional contributions unless your new job is with the federal government.

## A SERIOUSLY BAD IDEA

It's legal to withdraw your vested account value from the TSP when you leave the military. But if you do, you'll pay the income tax that's due, plus a 10% tax penalty if you're not yet 59½, and wipe out your savings for the future. So it's never a good idea.

**Option 2:** You can roll over your account value to an individual retirement account (IRA) when you leave the military or at any point in the future. The preferable method is to authorize a direct transfer from the TSP to the IRA trustee or custodian. You'll want to choose a custodian that offers the types of investments you want to make and charges modest fees.

**Option 3:** You can have your account value transferred from the TSP to a new employer's plan, but only if that plan accepts transfers. You'll want to be sure the new plan offers comparable investment alternatives at comparable cost.

Look for an adviser who holds the CFP designation from the Certified Financial Board of Standards, the ChFC designation from The American College, or is a fee-only adviser who is a member of the National Association of Personal Financial Advisors (NAPFA). The advice won't be free, but it can be invaluable.

## THE LUMP-SUM QUESTION

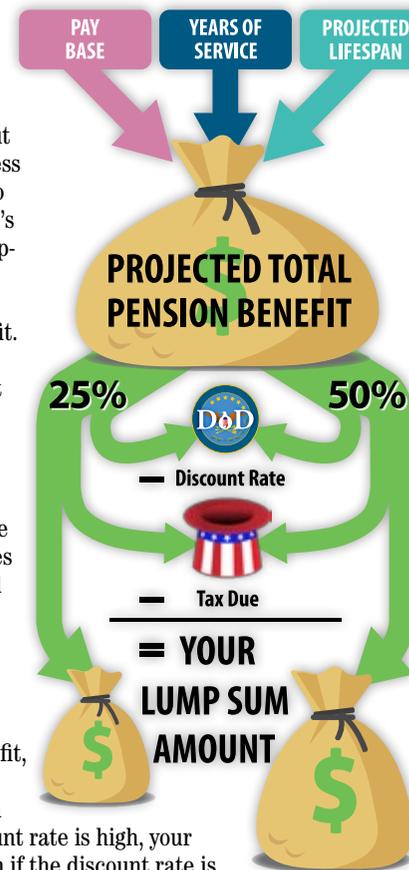
There's one feature of the BRS that doesn't require an immediate decision, but which you'll need to address if you serve long enough to qualify for a pension. That's the option of taking a lump-sum payment at the time you retire of either 25% or 50% of your pension benefit. In exchange, you agree to a reduced monthly benefit until you turn 67.

To calculate your pension benefit, or the total of the monthly amounts you would receive in retirement, the DoD uses your pay base, determined by your High-3 base pay and years of service, and your projected lifespan.

The lump sum you are entitled to will be 25% or 50% of that projected benefit, reduced by a factor called the **discount rate**, which the DoD sets. If the discount rate is high, your lump sum will be less than if the discount rate is low. But either way, the actual lump-sum amount you receive will be smaller than the percentage of your pension benefit you've selected.

One downside of taking the lump sum is that you'll owe income tax on the full amount you receive, which could jump you into a higher income bracket and increase the rate at which the tax you owe is calculated. However, you may choose to take the payout in installments over several years, which would reduce the tax due each year and perhaps the total tax you owe.

As in other cases where you're making an irrevocable decision about a retirement option, you'll probably want to seek professional advice from a military financial counselor or a private-sector adviser with comparable credentials.



## TIME TO WITHDRAW

The time will come when you must start withdrawing from your tax-deferred TSP account, or from the IRA or employer plan into which you have rolled your TSP assets. In nearly every case that will be by April 1 of the year following the year you turn 70½. From a tax perspective, though, it almost always makes financial sense to take the first withdrawal in the year you actually turn 70½. That way, you avoid having to take two withdrawals in the second year and pay tax on the combined amount.

Generally, your retirement plan administrator or custodian will notify you of the amount you need to withdraw for the year. That amount is based on a formula that divides your account balance at the end of the previous calendar year by a factor called the distribution period, which is determined by your age. You can find this information in Table III of *IRS Publication 590*.

## TERMS OF RETIREMENT

When retirement assets are moved between accounts by plan officials, it's technically a **transfer**. When you handle the move yourself, it's a **rollover**. But in common usage, when money is moved from one tax-deferred account to another, it's described as a rollover. Similarly, when you take money out of your account, it's technically a **distribution** but is universally known as a **withdrawal**.

# In the Reserves

The winds of change have picked up speed.

The Blended Retirement System (BRS), which went to effect on January 1, 2018, introduced some major changes for members of the National Guard and Reserve component.

The BRS has two key features:

- A tax-deferred retirement savings plan, including a DoD contribution, that is open to everyone who joins the armed forces and is receiving pay.
- A pension for members who complete 20 years of qualifying service, calculated as 2% of retirement base pay.

## RETIREMENT SAVINGS

Everyone who joins the Reserves or National Guard for the first time and is eligible to participate in the retirement savings plan is automatically enrolled in the federal government's Thrift Savings Plan (TSP). The DoD opens an account in your name and makes a contribution each pay period of 1% of your base pay starting on your 61st day of

service. That contribution is in addition to what you're earning.

As soon as your account is opened you begin making contributions that are automatically deducted from your earnings each pay period and deposited in your TSP account. After you've completed two years of service, the DoD will begin matching your contribution, up to 5% of your base pay. So every pay period you contribute 5%, the DoD will add 5%—the automatic 1% plus 4% in matching money.

The DoD sets the initial rate—3%—at which you contribute and chooses the initial investment, which is the L2050 lifecycle fund. You can stick with that default rate and investment choice throughout your career or you can change them. For example, you may decide to invest in one or more of the other funds available in TSP.

You do have the right to opt out, and not participate, but only after you complete a course in financial education.



## CALCULATING YOUR PENSION

The amount of your pension as a Reserve member depends on your equivalent years of service and is calculated in three steps.

1. Equivalent years are determined by dividing the total points you accumulate over the 20 or more years of qualifying service by 360.
2. The result is multiplied by the pension multiplier—2% under the BRS—to find your **retired pay multiplier**.

3. Your retired pay multiplier is multiplied by your retirement pay base to find your monthly pension amount.

You can increase your pension if you join the Retired Reserves when you retire. That way the base pay for your rank that applies when you turn 60 will be higher than the amount for your rank at the time you retired. Remember, though, that as a member of the Retired Reserves you could be called back to active duty or the Ready Reserves.

## SOMETHING TO CONSIDER

As a Reserve member who may be part of a civilian employer's 401(k) or similar retirement savings plan, you'll want to be aware of a potential complication of participating in the TSP. That's because you're entitled to contribute up to the annual cap that Congress sets for these plans—\$18,500 for 2018—across all TSP, 401(k), 403(b), or 457 plans in which you participate. (An employer's matching contribution doesn't count against the cap.)

If you contribute more than the cap, you face a potential tax penalty for each year the excess

remains in your account. And keeping track of your contributions is strictly your responsibility. Employers don't monitor what you may be adding to a different retirement account.

One approach if you find yourself in this situation is to contribute just enough to the TSP to qualify for the full match and then set a dollar limit for your civilian employer's plan so that you reach but don't exceed the cap. If you have an equal amount withheld from your employer's plan each pay period, you may also qualify for that employer's full match, if there is one.

## CAREER CONTINUATION PAY

As a Reserve member participating in the BRS, you'll qualify for career continuation pay at some point between your eighth and twelfth year of service. The Secretary of your branch determines the timing and the amount you'll receive.

If you're in the Active Guard Reserve or a Full Time Support member, you're eligible for this bonus at the same rates that apply for active component members—between 2.5 and 13 times your monthly pay base. As a condition of receiving the bonus, you must agree to serve the required additional time in the Select Reserve.

If you're serving in other Reserve categories, you're eligible for continuation pay calculated with multipliers between 0.5 and 6 times the monthly pay base.



**Asset allocation** is a strategy for investing in different asset classes, such as stocks and bonds, to help manage investment risk without sacrificing the potential for a strong return. But asset allocation does not guarantee investment gains or protect against losses in a falling market.

**Base pay** is the amount you earn each month. It does not include housing and other allowances that are part of your total compensation or any additional benefits or special pay. Base pay is also known as basic pay.

**Blended Retirement System (BRS)** is the military retirement system that took effect on January 1, 2018. It combines a pension with a retirement savings plan that features an automatic DoD contribution of 1% of base pay for all service-members plus a matching contribution of up to 5% of base pay if you contribute to a Thrift Savings Plan account.

**Career continuation pay** is an incentive payment available to all BRS participants at some point between your eighth and twelfth year of service at the discretion of the Secretary of your service branch. As a condition of the payment, you agree to serve three additional years.

**Compounding** occurs when investment earnings are added to investment principal, creating a new, larger base on which future earnings are calculated.

**Diversification** is a strategy for managing risk and enhancing return that involves buying a number of different investments within each asset class. But diversification does not guarantee a profit or protect against losses in a falling market.

**Index** is a list of investments that share one or more relevant characteristics, such as asset classification, market capitalization, or investment objective, and whose changing collective performance is an indication of how that segment of the market is performing.

**Individual retirement account (IRA)** is a retirement savings plan you set up with a financial institution. Your IRA earnings grow tax-deferred

and are reinvested to help build your account value. You can choose between a traditional tax-deferred account and a tax-free Roth account.

**Lifecycle funds** are intended to provide a source of retirement income starting at a specific future time, such as 2040 or 2050. Each lifecycle fund gradually shifts its investment emphasis from growth to income as the target date approaches.

**Portability** means that you can move investment assets you have accumulated in one retirement savings plan to another plan without losing their tax-deferred status. For example, when you retire or leave the service for any reason, you can move assets in a TSP account to an IRA or to another employer's plan if the plan accepts transfers.

**Retirement pay base** is the amount on which your pension is calculated in the Blended Retirement System. It depends on your High-3, or average base pay during the 36 continuous months it was the highest and the date you joined the armed forces.

**Return** is the gain or loss on your investment principal. It is determined by the change in an investment's price over a specific period, such as a year, plus any earnings the investment provides.

**Tax-deferred** means that any taxes that would otherwise be due on earnings in a retirement savings account are postponed until you withdraw money from the account. In some accounts, taxes are also deferred on contributions you make to the account. Annual withdrawals are required from tax-deferred accounts after you turn 70½.

**Tax-free Roth** is a retirement savings account in which earnings are tax deferred and withdrawals are tax free provided you are at least 59½ and your account has been open at least five years. Contributions are never tax-deferred. Withdrawals are required after 70½ from an employer plan Roth account but not from a Roth IRA.

**Vesting** means you are eligible to receive income from your employer's retirement plan or plans, based on having completed the required years of service. Vesting periods differ in different types of plans.



*Guide to the Military's Blended Retirement System* was developed in collaboration with and funded by the Defense Credit Union Council, a non-profit, niche trade association supporting credit unions operating on military installations worldwide.

As a chartered member of the Department of Defense Financial Readiness Campaign, the DCUC maintains a close and constant liaison with the DoD, coordinating on matters impacting financial quality of life, financial capability, and financial products and services, including financial education offered by on-base credit unions to military and DoD civilian personnel and their families.

DCUC is the primary spokesperson at DoD for federal and state chartered credit unions operating on base, functioning in this capacity and serving in this role since 1963.

[www.d cuc.org](http://www.d cuc.org)

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## SPECIAL THANKS

Anthony R. Hernandez, President and CEO, and Christopher Cosby, SVP of Operations, Defense Credit Union Council  
Roland "Arty" Arteaga, former President and CEO, Defense Credit Union Council

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Tel. 212-485-8800  
ISBN: 978-1-933569-15-4

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# GUIDE TO THE MILITARY'S BLENDED RETIREMENT SYSTEM

is the essential guide to the Department of Defense's new retirement initiative. The guide clearly describes the key features and benefits of the new approach, including the tax-deferred TSP account, matching contributions from the DoD, and investment choices and strategies for building a retirement portfolio.

## Spotlight on TSP

You can find the information you need to make smart decisions.

The Federal Thrift Savings Plan (TSP) provides access to a wide variety of investment options across a wide range of asset classes and other government securities. And the TSP gives you a broad base for investing in the Plan and a broad base for receiving your TSP benefits from either an immediate or deferred annuity.

**INVESTING MADE SIMPLE**  
One of the great benefits of automatic enrollment is that it simplifies decision-making. The initial

rate at which you contribute and the only your money is invested in one of the funds. You have the right to contribute to a wider or lower rate. Of course, if you want your account value to grow faster, there is the way to go. Similarly, if you would rather put your money into the individual funds offered in the TSP, you can make the switch whenever you're ready.

## TRADITIONAL OR ROTH

**CHOOSING A ROTH**  
One change you might consider right now is making your contributions to a tax-deferred Roth account rather than the default tax-deferred account. The TSP allows you to make the automatic change to a ROTH account. This change is subject to a 5% reduction in the amount of your contributions that you make to a Roth account.

It's important to understand that you can't reduce your account balance or the amount you owe. However, you can choose to invest in the Roth account. You'll have to pay taxes on the money when you withdraw it, but you'll avoid the 10% penalty on early withdrawals. You'll also avoid the 10% penalty on early withdrawals. You'll also avoid the 10% penalty on early withdrawals.

fully lower rates, and more money in your pocket, during retirement. And while contributions are not required from the default tax-deferred account, you are required to contribute to a Roth account. If you want to take advantage of both, you can contribute to both a traditional and a Roth account. For example, you can contribute \$500 to a traditional account and \$500 to a Roth account. The only limitation is that the combined total



### BLENDED RETIREMENT SYSTEM

**INDIVIDUAL FUNDS**

**Index Mutual Funds**

**TSP INVESTMENT CHOICES**  
If you elect with the default investment, your contributions will be allocated to the L2010 Fund. If you elect to invest in a different fund, your contributions will be allocated to that fund. For example, the L2010 Fund has 87% of its assets in stock funds, while the L2040 Fund has just 41% in stock funds.

**TAKING A TARGET**  
The TSP offers a target benefit plan called the Target Benefit Plan. This plan is designed to provide a steady stream of income during retirement. The Target Benefit Plan is designed to provide a steady stream of income during retirement. The Target Benefit Plan is designed to provide a steady stream of income during retirement.

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THE FINANCIAL  
EDUCATION COMPANY

ISBN 978-1-933569-15-4  
9 781933 569154