

MQFP® Study Guide 1.9: Active-Duty Retirement Planning

Learning Objectives:

1.9 Active-Duty Retirement Planning

a. List and describe each of the TSP funds

Five funds available: G Fund, F Fund, C Fund, S Fund and I Fund. Also have Lifecycle Funds with different ending years (Target Date funds).

G Fund (Government Securities Investment Fund) - most conservative fund. 'Ensure preservation of capital and generate returns above those of short-term US Treasury Securities'. Lifetime return 4.66% (as of 12/2023)

F Fund (Fixed Income Index) - 'Match the performance of the Bloomberg US Aggregate Bond Index'. Lifetime return 5.27% (as of 12/2023)

C Fund (Common Stock Index) - 'Match the performance of the Standard and Poor's 500 (S&P 500) Index'. Lifetime return 10.69% (as of 12/2023)

S Fund (Small Cap Stock Index) - 'Match the performance of the Dow Jones U.S. Completion Total Stock Market Index'. Lifetime return 8.57% (as of 12/2023)

I Fund (International Stock Index) - 'Match the performance of the MSCI EAFE (Europe, Australasia, Far East) Index'. Lifetime return 4.82% (as of 12/2023). Most aggressive/risky fund.

Exercise 1: TSP Fund Description

Provide a detailed description of each of the Thrift Savings Plan (TSP) funds, including their investment objectives, risk levels, and historical performance.

b. Analyze and contrast TSP Lifecycle funds for a client situation

- If client age 20's to 30's, potential portfolio - 40% C Fund, 30% S Fund, 20% F Fund, 10% I fund
- If client age 40's to 50's, potential portfolio - 35% C Fund, 20% S Fund, 40% F Fund, 5% I Fund
- If client age 60's to 70's, potential portfolio - 20% C Fund, 15 % S Fund, 35% F Fund, 30% G Fund

Exercise 2: TSP Lifecycle Fund Analysis

Analyze and contrast TSP Lifecycle funds based on a hypothetical client's age, risk tolerance, investment horizon, and retirement goals.

c. Describe the modes and limitations of TSP distributions

Lump-Sum Payment: This option allows you to take all or part of your TSP account balance as a single payment. However, taking a lump-sum distribution may have tax implications, and the entire amount withdrawn becomes taxable income in the year it's withdrawn.

Annuity: The TSP offers annuities, which are a series of monthly payments made to you for life or a specific period. An annuity can provide a steady income stream, but it's important to carefully consider the terms and conditions of the annuity before choosing this option.

Systematic Withdrawal Payments: With this option, you can set up regular monthly, quarterly, or annual payments from your TSP account. You have control over the frequency and amount of these payments within IRS guidelines.

Transfer or Rollover: You can transfer or roll over your TSP funds to another eligible retirement plan or IRA (Individual Retirement Account) without incurring taxes. This option allows you to maintain the tax-deferred status of your retirement savings.

Leaving Money in the TSP: If you're satisfied with the TSP's investment options and fees, you can choose to leave your money in the TSP even after you retire or separate from federal service.

Exercise 3: TSP Distribution Modes and Limitations

Describe the various distribution options available from the TSP, including partial withdrawals, annuities, and required minimum distributions (RMDs). Explain any limitations or tax implications associated with each option.

d. Contrast the military's legacy ("High 36") retirement system to the blended retirement system (BRS) and calculate the expected retired pay under each system given a set of client circumstances

1. Military Legacy Retirement System:

- Eligibility: This retirement system primarily applies to service members who entered the military before January 1, 2018.
- Structure: It follows a traditional pension-based system, where service members receive a defined benefit based on their years of service. The pension amount is calculated based on the average of the highest-paid 36 months of service and a multiplier (generally 2.5%) multiplied by the number of years served.
- Vesting: Service members become eligible for retirement benefits after completing at least 20 years of active-duty service.
- Additional Benefits: Alongside the pension, members may be eligible for other benefits, such as Tricare for life, commissary and exchange privileges, and other retirement-specific benefits.

● 2. Blended Retirement System (BRS):

- Eligibility: This system applies to service members who entered the military on or after January 1, 2018.
- Structure: It combines a reduced defined benefit pension with a government-matched Thrift Savings Plan (TSP) contribution.
- Defined Benefit: The pension component is a reduced version compared to the legacy system, calculated at 2.0% instead of 2.5% for each year served, based on the highest-paid 36 months.

- Thrift Savings Plan (TSP): The BRS includes a TSP with automatic and matching government contributions. Service members receive automatic government contributions of 1% of their base pay into the TSP, and after two years of service, they become eligible for additional matching contributions of up to 5% of their pay.
- Vesting: The vesting period for the TSP contributions is immediate, while the defined benefit pension requires a minimum of 20 years of service for eligibility.
- Opt-In Choice: Service members with fewer than 12 years of service as of December 31, 2017, were given the choice to opt into the new BRS or remain in the legacy retirement system.

Comparison:

- *Pension Structure:* The legacy system offers a higher percentage for the defined benefit pension (2.5% per year) compared to the BRS (2.0% per year). However, the BRS includes a TSP with government contributions, providing potential additional retirement savings.
- *Eligibility:* The BRS includes a TSP with government contributions for all service members, while the legacy system only benefits those serving before 2018.
- *Opt-In Choice:* Service members had the option to switch to the BRS if they qualified, considering their individual circumstances and preferences.

Both systems have their merits and drawbacks, and the choice between them depends on various factors such as individual career goals, length of service, and retirement savings preferences.

Exercise 4: Retirement System Comparison and Calculation

Compare the military's legacy "High 36" retirement system to the Blended Retirement System (BRS), considering factors like pension calculation methods and TSP contributions. Calculate the expected retired pay under each system for a client based on their years of service, rank, and pay.

e. Calculate TSP employer matching contributions under the BRS

Employee Contributions: Employees enrolled in the TSP can contribute a portion of their salary to the plan on a pre-tax or after-tax basis, up to the annual IRS limits.

Matching Contributions: For eligible participants, the government (the employing agency) may provide matching contributions to their TSP accounts. This is essentially free money that the government contributes to an employee's retirement savings.

Matching Contribution Formula: The matching contribution formula can vary based on the employing agency and the specific plan. The most common match is the "1% for 1% match" where the agency matches the employee's contributions up to 1% of their salary and then matches 50 cents on the dollar for the next 4%.

Vesting: Matching contributions made by the government may be subject to a vesting schedule. Vesting refers to the amount of time an employee must work in a job before gaining ownership of employer-contributed funds. For federal employees, the TSP has a vesting period of three years, meaning employees are fully vested in the agency's contributions after completing three years of federal service.

Limits and Regulations: There are limits on the maximum amount of matching contributions an employee can receive, as set by the IRS. The IRS may also impose restrictions on the types of contributions, the timing of contributions, and other regulations governing retirement plans.

Exercise 5: TSP Employer Matching Contributions

Calculate the TSP employer matching contributions under the Blended Retirement System (BRS) for a client based on their TSP contributions and the applicable matching percentage.

f. Summarize the automatic enrollment policy for BRS

Automatic enrollment works by enrolling eligible employees into the TSP unless they choose to opt-out. When a new employee becomes eligible to participate in the TSP, they are automatically enrolled at a default contribution rate (typically a percentage of their salary). This default contribution rate is set by the employer or the plan and can vary.

The automatic enrollment process aims to increase retirement savings participation rates by simplifying the decision-making process for employees who may otherwise not take action to enroll in the retirement savings plan. It helps employees start saving for retirement without having to take the initial step of actively signing up for the plan.

Employees who are automatically enrolled have the option to change their contribution rate, investment options, or opt-out of the plan altogether if they wish to do so. Automatic enrollment serves as a helpful tool to encourage retirement savings but allows flexibility for employees to adjust their contributions based on their financial goals and circumstances.

Exercise 6: BRS Automatic Enrollment

Summarize the automatic enrollment policy for the Blended Retirement System (BRS) and explain its implications for newly enlisted service members.

g. Explain the BRS lump sum option and BRS continuation pay

The military Blended Retirement System (BRS) introduced new retirement benefits for service members that took effect on January 1, 2018. As part of the BRS, there are two components related to lump sum and continuation pay:

Lump Sum Option: At the completion of a service member's 12th year of service, they have the option to receive a lump sum payment. This payment is equivalent to 2.5 times their monthly basic pay. However, in return for this lump sum payment, the service member agrees to receive a reduced retirement annuity. This lump sum option is one-time and is offered to individuals in exchange for a slightly reduced retirement pay.

Continuation Pay: This is an additional incentive designed to encourage service members to commit to serving longer in the military. It's a one-time bonus offered to members who reach certain points in their career (usually around 12 years of service) and agree to commit to an additional service obligation (typically four more years). The continuation pay bonus amount varies based on the branch of service and career field, but it can be a significant amount, up to 13 times the monthly basic pay.

Exercise 7: BRS Lump Sum and Continuation Pay

Explain the BRS lump sum option, including the conditions under which service members can receive a portion of their retirement pay as a lump sum. Describe BRS continuation pay and the requirements for eligibility.

Quiz: (Multiple Choice)

1. Which TSP fund primarily invests in government securities and is known for its stability and safety?
 - a) C Fund
 - b) S Fund
 - c) I Fund
 - d) G Fund

2. True or False: TSP Lifecycle funds are designed to maintain a fixed asset allocation throughout the investor's lifetime.
 - a) True
 - b) False

3. What are the main modes of TSP distributions available to participants?
 - a) Partial withdrawals, life annuities, and required minimum distributions (RMDs)
 - b) Full withdrawals and monthly payments
 - c) Life annuities and TSP loans
 - d) Required minimum distributions (RMDs) only

4. Under the Blended Retirement System (BRS), what percentage of a service member's basic pay can they receive as employer matching contributions?
 - a) 3%
 - b) 4%

c) 5%

d) 6%

5. True or False: Newly enlisted service members are automatically enrolled in the TSP with a 1% default contribution rate under the Blended Retirement System (BRS).

a) True

b) False

References:

- Thrift Savings Plan (TSP), Federal Retirement Thrift Investment Board: <https://www.tsp.gov/>

- Blended Retirement System (BRS), Military Compensation:

<https://militarypay.defense.gov/BlendedRetirement/>

*Answer Key can be found at: <https://mqfp.org/study-guides/8> *