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SmartMoney
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Here's How to Double Your Nest Egg

KIM NORTON DUTIFULLY contributed to 401(k)-type plans for almost 20 years, routinely hitting the maximum contribution ceiling as she built a six-figure nest egg. But the aftermath of the tech bubble convinced her she'd need a bigger security blanket. So the Denver real-estate agent tore up the savings playbook; she started buying property with her IRA funds and flipping it to earn big returns. It's more risky than traditional retirement investing, but Norton's willing to take bigger risks for higher rewards—especially now that she's resolved to build her savings to $2.5 million.

The current economic climate offers many reasons to be legitimately worried about financing retirement. Soaring fuel, food and health-care costs have reminded everyone how badly inflation can hurt a fixed income, and the ongoing credit crisis and the falling stock market have made investors realize how fragile a nest egg can be. But many people are still finding ways to throw their future a life raft. SmartMoney talked to several retirees and soon-to-be retirees who managed to double their retirement savings within an eight-to-10-year period. We examine two approaches below; for more, pick up the October issue of SmartMoney magazine.

Redefining the IRA

Why not put a fleet of limousines or a rental beach cottage in your retirement account? Tens of thousands of Americans are doing something similar with a "self-directed" IRA. These arrangements allow investors to use retirement assets to buy almost anything that generates a stream of income, provided the income flows right back into their retirement account. Only about 2 percent of the $5.7 trillion IRA market is in such investments, but bigger providers of self-directed IRAs report double-digit annual percentage growth in the number of accounts.

Two years ago, Kim Norton used a self-directed IRA to scoop up a unit in a soaring luxury-condo complex in Denver. She sold it this year, landing a 114 percent return on her investment. "It's all kind of exhilarating," she says. But along with that exhilaration, the do-it-yourself market can pose big risks. Most investors, for example, use them to buy real estate—and in the current crash, many took painful losses. Even more important: There has to be a strict divide between IRA and personal funds. Self-directed investors can't materially benefit from their IRA purchases—if your IRA owns a limo fleet, you can't use it to loan a car to your kid for prom. And they can't spend non-IRA assets on an IRA investment—not even to pay the cleaning lady at a rental property. One misstep on these fronts and the investor faces big tax penalties. These hurdles explain why the law requires that investors hire "custodian" companies to handle self-directed IRAs. Investors can lean on these firms for advice about the dos and don'ts.

The Small-Business Secret

Six years ago, retirement seemed almost out of reach for Bob and Susan Hansen. Although Bob earned a healthy salary as an aerospace executive, the couple's nest egg barely cracked six figures. Their solution: In 2005, Bob launched a small consulting firm that advised small aerospace firms on mergers. And he gave the firm a defined-benefit plan—the sort of old-school pension associated with the good old days of corporate America. Soon he and Susan were setting aside nearly all their business income, as much as $200,000 annually, in tax-deferred retirement accounts. They've relocated to a sprawling ranch in Montana, and in a year or so, Bob hopes to be fully retired. "It just all fit together for us," Bob says, "like a jigsaw puzzle."

Almost one in six small-business owners started his enterprise after age 45, according to recent research. And if a business does very well and generates enough surplus revenue, the owner can start a supercharged pension plan. Compared with 401(k) plans, these arrangements have virtually no contribution limits. (There is a ceiling on how big the accounts can grow—it's currently $2.2 million.) Fewer than 1 percent of small businesses use these plans, but a 2006 pension reform law made them easier to set up. Still, they aren't for everyone, cautions Ted Gregory, a Huntington Beach, Calif., certified financial planner who advised the Hansens. Among other things, you'll have to pay actuaries to revise your plans if your year-to-year contributions are erratic.

Not interested in becoming a part-time pension accountant? Self-employed people still have plenty of attractive savings options. While corporate types face 401(k) contribution limits of up to $20,500 a year, the self-employed can contribute 25 percent of their income, up to $46,000 each year, to Keogh or Simplified Employee Pension plans. With solo 401(k)s, which are available to businesses with just one full-time, adult employee plus spouse, people age 50 and over can contribute up to $51,000 a year, and the 25-percent-of-income cap goes away.

For more SmartMoney Magazine features, turn to the *October issue*[1].

4 Ways to Double Down

Running a Business

Creating a pension plan helps business owners and the self-employed sock away more tax-deferred cash for retirement. How to get in on the bounty:

Seek Help. Creating a plan requires the worker to commit to a payment schedule for himself and any eligible employees. Financial advisers can connect clients with an actuary who can design such a schedule, and companies like the San Francisco-based Dedicated Defined Benefit Services can devise simple, two-page pension contracts after phone consultations. Some major banks offer a similar service.

Watch the Math. Karen Shapiro, CEO of Dedicated Defined Benefit Services, says the plans usually make the most sense for consultants or business owners like doctors who are making more than they need to cover expenses and costs of living. It also helps to be older than 45, because actuarial formulas allow people closer to retirement to contribute more. The site *www.onepersonplus.com*[2] allows users to determine roughly how much they can sock away each year.

Get Creative. In some cases, a person can put 100 percent of his income from a business into a pension plan. Examples Shapiro cites include a small-business owner whose spouse's income supports the family and people who earn supplemental income from sources outside their regular work -- royalties from a book, for instance. Pension money can also eventually be rolled over into a traditional IRA.

Scaling Back Retirees can effectively increase the value of their savings by learning to live well on less money. How to do it gracefully: **Research the Big Stuff**. Homes and cars are most people's largest expenses. Shoppers can get a sense of the true cost of owning one type of vehicle versus another -- including maintenance, gas and depreciation costs -- at the car-oriented Web site Edmunds.com. The site can also help you weigh the pros and cons of buying a used car. For folks considering relocating to a new city, *Sperling's Best Places*[3] offers cost-of-living information for each zip code, including side-by-side comparisons of multiple locations, with a particular emphasis on housing costs. **Rent Instead**. Selling a home and renting can sometimes be a better deal than holding on to a home, says San Francisco-based wealth adviser Spencer Sherman, especially for folks who can invest the proceeds of the home sale. Would-be retirees can also sometimes stretch their nest egg by investing the difference between the cost of renting and the cost of owning. To evaluate whether it's a better idea to rent or buy a given property, calculate what percentage of the home's value you'd pay in annual rent for a similar home. If it costs more than 5 percent to rent, and you intend to stay a while, buying is the better deal.
Self-Directed IRA A self-directed IRA allows consumers to use retirement money to invest in real estate, small businesses or other alternative assets, as long as the income or returns they generate flow back into the IRA. How to profit: **Know the Rules**. Investments can't directly benefit the account holder or his family -- so no taking vacations in the cottage you purchased with IRA money, for instance. Any upkeep or bailout costs associated with an IRA investment must be paid from the same IRA account. The rules matter: Violators could face income taxes on their entire IRA balance and an additional 10 percent penalty if they're younger than 59 1/2. **Hands Off**. The law requires self-directed IRA investors to manage their investments at arm's length. Most experts suggest using one of the large self-directed IRA custodians like Entrust, Equity Trust or

Pensco Trust to handle income and payments related to the investment. Those services aren't free: Entrust, for example, charges $95 for each buying and selling transaction and a $250 yearly fee. Most custodian companies kick in educational materials and phone support.

Prepare for Taxes. Account holders can take out loans to finance IRA investments, but there'll be tax consequences. If loans paid for 50 percent of your investment, for example, you could owe income tax on 50 percent of your profit when you sell.

Waiting to Retire

Even a small delay in leaving the workforce can substantially boost a person's retirement income. Here's how to make waiting palatable:

Calculate the Benefits. The Social Security Administration's Web site can demonstrate how much larger a retiree's annual payout will be if she opts to take Social Security later than age 62. Sophisticated planning tools like ESPlanner or FIRECalc -- both available online -- help consumers see how the Social Security timing affects their retirement-savings goals.

Get a Fun Job. Various Web sites boast job postings that focus on retired workers. RetirementJobs.com, RetiredBrains.com and Seniors4Hire.org post listings for jobs of all kinds; the latter site, for example, prominently features ads for floral arrangers and schoolteachers. Another site, YourEncore.com, primarily connects retired scientists and engineers with part-time gigs at companies like Eli Lilly and Boeing.

Score a Pension. Typically, federal employees need to work only five years to qualify for a pension and lifetime health care. Second-career teachers can also earn significant pensions. Roman Franklin, a financial adviser in Deland, Fla., says Rhode Island and Georgia offer particularly competitive packages. One big "but": School systems in some states don't participate in Social Security, and that can result in lower benefit checks -- potentially offsetting the value of the pension. Job-seekers can learn more from the *National Council on Teacher Retirement*[4].

[1] http://www.smartmoney.com/mag/

[2] http://www.onepersonplus.com

[3] http://www.bestplaces.net

[4] http://www.nctr.org

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