A guide to your payout options

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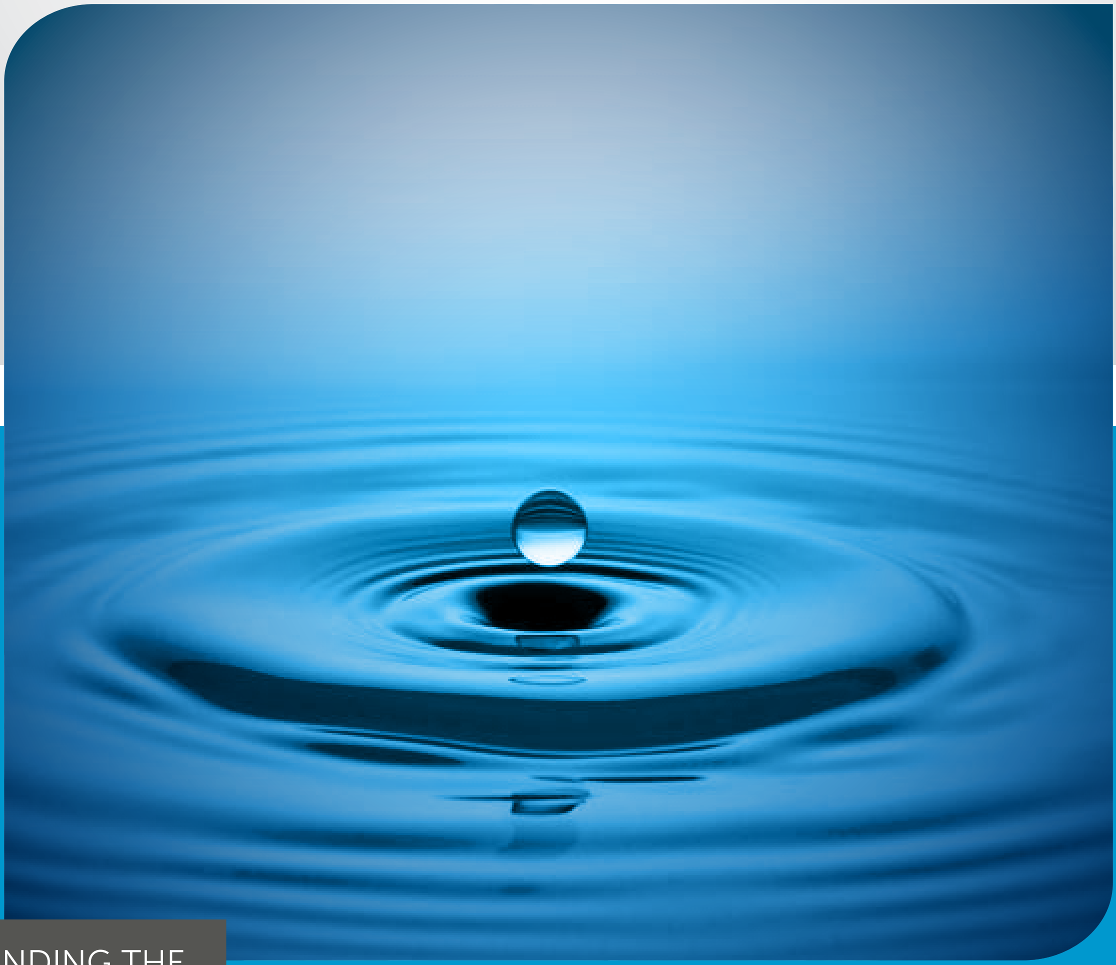

UNDERSTANDING THE

FLORIDA RETIREMENT SYSTEM'S

DEFERRED RETIREMENT OPTION PROGRAM (DROP)

Dedicated to helping Florida educators, public safety officers and public employees retire on their terms.

FLORIDA PENSIONERS

HAVE ACCESS TO THE DEFERRED RETIREMENT OPTION PROGRAM, OR DROP, AN INNOVATIVE PROGRAM THAT BENEFITS PUBLIC EMPLOYEES, TAXPAYERS AND THE ECONOMY.

How DROP works

DROP accruals are self-funded by retirees. If you are a retirement-eligible Florida Retirement System (FRS) participant, you can elect to join DROP and, depending on your employer, continue to work for five to eight years. During that time, you would get the same salary, raises, promotions and benefits as non-eligible employees, but will have retired from the pension plan. Instead of the pension payments coming to you, those payments will be paid into a pre-tax qualified retirement plan on your behalf. The pension plan pays 1.3 percent interest into the DROP.

When you decide to separate from service, you can roll your DROP money into a tax-qualified account, take a lump sum distribution or do a combination of both.

How DROP benefits public employees

Many public employees have not saved adequately for retirement, so the extra DROP accrual helps make up for a shortfall of savings. As of September 2016, the average DROP accrual balance is $146,039, with balances ranging from a few thousand dollars to more than $1 million.

How DROP benefits taxpayers and the economy

Our firm has helped thousands of Florida public employees save for a comfortable retirement that may not have been possible without DROP. Because a DROP participant must retire after five to eight years, the number of public employees in Florida with 40 to 50 years of service has been cut significantly.

What's more, when a participant exits DROP, he or she is usually at the top of the pay scale. The person who replaces the retiring participant is usually entry-level, often making 50 to 70 percent less, which lessens the burden on taxpayers and helps the economy by opening up new jobs.

THREE DROP

PAYOUT OPTIONS

As a participant in the Florida Retirement System's DROP program, you have three payout options when separating from service. You can elect an option on the DP-PYT form, which is located in your DROP exit packet. You usually will receive a DROP exit packet three to four months before exiting DROP.

The DROP payout option is one of the most important financial decisions you will ever make, so let's review the three options:

1 DROP Payout Option No. 1: "I Love Uncle Sam"

The first payout option is a lump sum cash-out. The DROP account is pre-tax money, meaning that a distribution is a taxable event. The FRS will send 80 percent of your total DROP balance to you, and 20 percent of the total DROP balance to the IRS for taxes. Our office lightheartedly refers to this option as the "I Love Uncle Sam" option because of its tax regulations.

Remember: Your tax bracket is determined on the amount of income you earn per year. So if you take a large taxable distribution in one year plus wages and retirement income, you may end up in a higher tax bracket than the 20 percent that is withheld and sent to the IRS. THE 20 PERCENT WITHHELD DOES NOT INCLUDE ADDITIONAL TAXES YOU MAY OWE AFTER DISTRIBUTION. Some individuals have unknowingly chosen this option and then had unexpectedly high tax bills, so carefully weigh your options.

The most common reason someone chooses this option is to pay off a large bill or mortgage. However, the potential tax ramifications can usually be avoided by paying off those bills in three to five years. To help control your tax liability, you could place your money in a fixed and relatively "liquid" qualified account, and then take systematic distributions from it at your discretion.

If you're considering Option No. 1, please first consult a tax professional.

PAYOUT OPTIONS

2 DROP Payout Option No. 2: "Stop, DROP and Roll"

The second option is the 100 percent rollover, which is for anyone who doesn't want to have a taxable distribution at the time of retirement. For many people, the year they retire will usually be the highest tax bracket of their lives. People who choose this option can often take their distributions at a later date, when they're usually in a lower tax bracket.

A common misconception by both participants and financial professionals is that you can only roll your funds to one account. However, you may roll your DROP funds into as many accounts as you'd like by making copies of your DROP form and writing at the top of each one, "1 of 3" or "2 of 4," for example.

Before electing which type of pre-tax account in which to roll your money, consult with your financial professional. Here are a few things to take into consideration:

- Roth IRAs: If you roll your money to a Roth IRA, you must pay taxes on all the money you elect to have sent to that Roth (effectively choosing Option No. 1) in that year.
- With Roth accounts, you also can't touch the interest for the first five years, and you can't take a distribution until you're 59½ or older without a penalty. If you're considering this option, please consult a tax professional.
- Traditional IRAs: IRAs and Roth IRAs tend to offer the most investment choices available, which make them a popular choice for most retirees. It's important to note that you can't usually take distributions from an IRA until you're 59½ or older without a penalty. There is a way to take distributions from an IRA via IRS Rule 72(t), but you will then also limit access to those funds.
- 403(b) (aka TSA), 457 (aka Deferred Comp), and other employer plans: If you're retiring before age 59½, you may want to consider rolling some or all of your money to one of your employer plans so you can have access to your funds. However, please consult a financial professional because each type of account has a different rule for what age you can take distributions.
- You also can take a loan from most employer plans, allowing you to first access tax-free funds, and then repay yourself. The main drawback of these plans are the limited investment options. Also, you may have to request permission from your employer or their third party administrator (TPA) to be able to access your funds.
- Keep in mind that when you pick a rollover option, you will have to fill out the second page of the DROP Payout form (DP-PYT) to tell the FRS where to send the money. This second page must be filled out and signed by your financial professional, or the FRS will not send the check.

3 DROP Payout Option No. 3: "Alaskan Cruise"

The third option is the partial lump sum option, or a combination of the first two options. You let the FRS know how much you'd like to be sent to you as a distribution, and the rest of the money is rolled over to whatever qualified account you choose.

Some of the most popular reasons to choose Option No. 3 include:

- To take a dream vacation (hence, "Alaskan Cruise," a popular post-retirement trip)
- To pay off high-interest debt (credit cards, loans, etc.)
- To purchase a vehicle
- To boost savings
- To pay off a small mortgage

Keep in mind that you're taxed based on what you take out, not on what you receive. So if you want to receive $10,000, you have to take out $12,500 ($12,500 – 20 percent tax withholding = $10,000).

Also, remember that your first pension check will not come until the month after you separate from service. So if you don't have enough money in checking/savings to pay for the next month's bills, you may want to consider taking out a partial distribution to get you to the end of the month.

Remember, any amount you elect to have paid to you as a distribution is taxable. That means that it will be added to your income for the year of the distribution, which may put you into a higher tax bracket. In addition, the 20 percent is just the withholding amount—you may owe more in taxes at the end of the year, or you may get a refund. Please consult a tax and/or financial professional if you're considering this option.

WANT TO LEARN MORE?

If you're interested in more information about the Florida DROP Program, please contact us at 888-960-4494. We can give you an objective opinion on options in line with your needs, goals and personal situation.

We've also created step-by-step instructions on how and when to fill out your FRS DROP or other FRS retirement forms. To access this information, please call 888-960-4494, email us at info@andersfg.com or visit our website at AndersFG.com.

Strategies for your financial independence

We know how important it is to take control over your future. At Anders & Anders Financial Group, we offer our experience and knowledge to help you design your own strategy for financial independence.

Contact us today to schedule a no-obligation Customer Care Needs Analysis. Call us at **888-960-4494** or connect online at **info@andersfg.com**. There is never an obligation on your part. If you can invest one hour today, we can place you on the path toward owning your tomorrows.

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