

Assignment 4 FN281: Retirement Planning

1) What types of expenses can be lowered or eliminated during retirement?

- **Commuting expenses:** Fuel for your vehicle or public transport fares cost a lot for employees. However, during retirement, retirees would drive less which helps them lower the expenses on fuel and fares.
- **Clothing expenses:** as some jobs require professional clothing that is no need during retirement.
- **Office costs:** Participation in office social life with coworkers, such as expensive business lunches, is important for employees but not anymore for retirees.
- **Paying full price:** retirees are qualified to get senior discounts for tourist destinations and car rentals.
- **Peak travel costs:** retirees can avoid traveling during peak seasons and get the cheaper price for airplane ticket or hotels.
- **High tax rate:** as retirees don't have salary which makes them fall into a lower tax bracket then pay less.

2) What types of expenses might increase during retirement?

- **Health care costs:** retirees may face higher health insurance premiums.
- **Traveling cost:** retirees have plenty of time to travel. By doing so, they may face an increase in expenses.
- **Socializing expenses:** since retirees have more extra hours, they can spend time on meals outside home or entertainment activities with friends.
- **Household help cost:** some seniors need assistance with home maintenance.

3) Explain the difference between a defined-contribution and defined benefit plan.

- **Defined –contribution plan**
 - Both employees and employers contribute to the funds. An employee, called the participant, puts money as a percentage of salary annually in pension account, and the employer matches contributions to a certain amount.
 - The participant can select to invest the contributions mutual funds, money market funds, annuities or stock offered by the plan.
 - The employee takes investment risk since retirement benefit amount depends on the account's performance that the employee chooses, and the employer does not have any obligation after the funds are deposited.
 - It is portable when the employee leaves the company
- **Defined benefit plan**
 - Employers promise a specified pension payment in retirement to employees.
 - Defined benefit plan is often based on the employee's salary, years of service or a number of other factors, such as age at retirement.

- Monthly benefit = Average salary x years of service x Z%
- The employees have little control over the funds and the plan can be changed by the company.
- The employer bears the investment risk of ensuring specific retirement benefit amount to the retired employee.
- It is not portable when the employee leaves the company.