Episode #252: Is Your Retirement Plan Government Sponsored or Privately Funded?

Video Transcription

Hello, my name is Sal Mendoza, and welcome back to "Money Script Monday." Today, we're going to be discussing is your retirement plan government sponsored or privately funded.

Before we get started, I just want to say I've been in this industry for 20 years, okay, and the most important thing today is for me to give you information so that you can make the best decision for yourself and for your family.

Let's get started with some of the questions. Some of the questions you should be asking yourself, okay, that you can ask your financial advisor is, how much money can you put into your retirement plan? Number two, can you borrow money from your plan?

Three, how long before you can start borrowing from your plan? Four, when must you start taking money out of your plan? And then finally, what tax rates, okay, will you have to pay when you start taking out that money?

So, I'm going to scoot over to my right here, and now we've opened up the board a little bit. And now you can really kind of see the contrast between a government-funded plan and a privately funded plan.

They're both excellent products, okay, they're both excellent products, it just depends on what you're trying to accomplish. I particularly have both.

Let's go over some of the highs and lows of each one. A government-funded plan is typically known as a 401(k), and a privately-funded plan is typically what we call a LIRP, a life insurance retirement plan. The first thing, easy setup, right, you start your job, you fill out one piece of paperwork, a couple of little checkmarks, a signature and date, and you're done in five minutes.

You've actually started your 401(k) plan. On a LIRP plan, a little bit more sophisticated, at least 15 pages, you have to qualify medically, and you have to qualify financially.

So there's a little bit more on a privately-funded plan. Limitations, the government limits how much money that you can put into the plan. As of 2022, it's $20,500. And if you're over 50, they allow an additional $6,500, so the ceiling is $27,000.

On the life insurance plan, okay, there is none, okay. There is no...it depends on how much you make, how much you financially qualify. I've seen these for $100,000 a year. I've seen these for $250,000 a year. I've also seen them $1,000 a week. Okay, so I've seen all kinds of different variations, it all depends on financial justification.

Next, on a 401(k), one of the big reasons, okay, for a company to retain employees, and to offer them better benefits is a match, I typically see around a 3% match, sometimes a little bit more.

By the way, if you have a company that's not matching you, you know what, I would probably walk into human resources and say, "Come on, give me a match." Right?

Most companies offer a match. They should be able to do that. Three percent is what I see. Anything above that, then you have a very generous, very caring company who's really trying to give you the most that they possibly can. And they should, they get a tax break when they do that. Okay?

In a privately-funded plan, you can see here, there is no match, okay, your dollar is working for dollars, there's no one... Because it's a privately-funded plan, you're doing your own plan. There's no company behind it.

However, you'll see that there's a little asterisk by that no match. And what's powerful about that is that we do have the ability, okay, to get you three-to-one leverage. So, $3 for every dollar you put in.

You need to speak to your financial advisor about premium finance. Okay. Next, is, you know, how do you actually start contributing to your government-funded plan?

Well, depending on what you chose, you know, let's say you chose 5%. That means that if you make $1,000, okay, that means $50 every paycheck, they're going to put into your plan. It's just really that simple, nothing more, nothing less.

Here, if you decide to set that up, you can set up to pay however you want. You can set it up to pay weekly, you can set up to pay monthly, semi-annually, quarterly, or annually.

You can even, like, if you have some money, and, you know, it's dependent on the design, of course, you can put in money every other week that's extra in addition to the money that's been pulled out of the EFT. So all I'm saying is there's a lot more flexibility in a LIRP plan compared to a 401(k) plan.

Market volatility, holy smokes, you can see where sometimes the market will go up and down. You know, we like it to do this, and it does that every, you know, eight years where it kind of goes up, but then there's always a significant pullback, you know, 15%, 20%, 25%.

It doesn't seem like a lot when you have a little bit of money, but when you have hundreds and hundreds and hundreds of thousands, and you have a 20% pullback, that's a pretty significant blow, right? So, that's the nature of this product.

So you're going to have anywhere from a minus 20, but you also have the upside of a plus 20 as well, too, and anything in between. All right. So nothing wrong with that.

There are a lot of things that you need to ask yourself, you know because you can help soften the blow depending on the ratios that you have your money in.

In a privately funded plan, you can have as much as 20%, but they have a unique feature there that is called a zero-floor. And that just means that if ever the market, okay, goes under zero, so, like, a minus 1, or a minus 5, or minus 10, you will never participate in any negative numbers, the worst number is going to be a zero, that is a huge incentive for you.

Lastly, a government-funded plan, 401(k) specifically, has no tax shield. Well, all that really means is one day, whether you're 59 and a half when you retire or 65 when you retire, and you start taking distributions out, you're going to have to pay taxes at the tax rate when you retire.

Let's just for a quick example, let's say that you've been contributing for 30 years at X company, and now you've accumulated a million dollars. And let's say your retirement tax rate is 30%.

That means that $700,000 is for you, and $300,000 goes to the IRS, very simple. In a privately-funded plan, you're going to notice that it has a tax shield. In fact, I put a tax shield up there.

The reason why it's a shield, okay, it's a firewall, and you don't have to pay any taxes in the growth of that money when you pull it out. Okay. Huge incentive of why you should consider opening a LIRP, in addition to your 401(k).

I believe in having a diversified portfolio. I've been doing this for 20 years. I believe in having money in real estate. I believe in having money in a LIRP.

I believe in having money in a 401(k). I believe in having money in annuity once you go over the age of 50 to consider that.

I believe in having money in maybe some commodities, gold, and silver, just in case, I believe in a diversified portfolio.

But it always starts with a lot of great questions to ask your financial advisor.

Hopefully, you got some insights into a government-sponsored plan versus a privately funded plan.

My name is Sal, thanks for letting me share.