The Exciting World of Tax Brackets! (And Why They Are Important To You Saving Money)

Scott A. T.: Broadcasting from one One Dallas Tower, welcome to the Financial Rock Star Show. I am your host, Scott Alan Turner, here to help you get out of debt, save more money, and retire early. In the studio with me is producer Katie, who's able to use chopsticks at an intermediate level. On the show today, I'll be answering your questions about money, business, and life. If you have a question you'd like answered on this show, visit goaskscott.com.

Here's an old article from HuffPo. It says, "For whatever reason, an article titled Investors Rush to Beat Threat of Higher Taxes, was published by the New York Times despite the fact that it contains a galling bit of stupidity, which could spread like a super virus to the general public. It is these three paragraphs in particular. Kristina Collins, a chiropractor in McLean, Virginia, said she and her husband plan to closely monitor the business income from their joint practice to avoid crossing the income threshold for higher taxes outlined by President Obama on earnings above two hundred thousand dollars for individuals, and two-hundred fifty thousand dollars for couples. Ms. Collins said she felt torn by being near the cutoff line and disappointed that federal tax policy was providing a disincentive to keep expanding a business she founded in 1998.

"'If we're really close, and it's near the end of year, maybe we'll just close down for a while, and go on vacation,' she said." Taxes. It's so exciting. I can't wait to hear about tax brackets. If you missed yesterday's show, I gave you a primer on why we're going to spend some time talking about taxes. If you haven't heard that, please go back and listen to that before we get into this.

If you understand tax brackets, two things. One, you have the opportunity to manipulate, in a legal way, how much money you'll pay in taxes, which saves you money. That is exciting. Number two, you'll be able to explain this to other people who may or may not understand it. If you're already familiar with tax brackets, how they work, this will just be more tools to help explain them, more tools to put in your tool bag.

We're going to be working on some eighth grade math here, maybe seventh, maybe sixth. If you successfully passed those grades, booyah, you're going to get this. Understanding tax brackets, we're doing our own little short segment because it's going to set us up for everything else when we talk about taxes. You're not going to be able to take advantage of future shows, future discussions on taxes unless you understand how tax brackets work. In the next show, we're going to talk about converting some of your tax deferred retirement accounts, like your 401k, 403b, Traditional IRA to non tax deferred like Roth IRA specifically, and paying, potentially paying zero dollars in taxes when you do that conversion.

To get there, we've got to understand tax brackets, and how they work. Most people, including most politicians, don't understand this. It's not hard. You're about to be more smarter than your average politician, which is not different. You've probably never heard this. It doesn't mean there's anything wrong with you for not knowing this stuff, because they don't teach it in school. They don't teach it anywhere, in fact. I'll give you just a basic example of the problem, and then the reality of what's going on. I've got to use big round numbers so you can follow along. We don't have a whiteboard. You might be running. You might be in the car. I'm not going to use ... We're using round numbers. Just put it that way.

If you're single, and we're going to be talking about a single person, ignoring a lot of the extra stuff that goes along this to make it really easy. If you're single, your taxable income is zero to ten thousand dollars, you pay ten percent in taxes. Ten thousand dollars in taxable income, a thousand bucks in taxes. On the dollars you earn between ten thousand dollars and thirty-five thousand dollars, say your salary is thirty-five thousand dollars, it's fifteen percent.

Dollars zero through ten are taxed at ten percent. Dollars ten thousand through thirty-five thousand dollars are taxed at fifteen percent.

Let's keep going. Thirty-five thousand dollars to ninety thousand dollars, if you're single, your taxable income is in that range. The dollars between thirty-five and ninety are taxed at twenty-five percent. Then between ninety thousand a hundred ninety-thousand dollars, if you're in that range, those dollars between ninety and one ninety are taxed at twenty-eight percent. Stop right there, because I'm probably already losing some of you. Those are four brackets and rates for a single person. Zero to ten thousand, ten percent. Ten thousand to thirty-five thousand dollars, fifteen percent. Thirty-five thousand dollars to ninety thousand dollars, twenty-five percent, and then ninety thousand to a hundred ninety-thousand, twenty-eight percent.

Those might sound a little familiar to you. At least the ten percent, fifteen percent, twenty-five percent, twenty-eight percent. You might be familiar with those percentages of taxes. Maybe not as much as with the ranges for each of those. Those ranges are called brackets. I'm going to ignore all the deductions. I'm ignoring the ten thousand page IRS code. You know it takes three hours plus to do a tax return. I'm just jumping to the bottom line in three seconds for this example. We can't get into all that.

Ninety thousand dollars, that was one of our cutoff points I just mentioned. Some people think they're paying twenty-five percent in taxes, which would come out to twenty-thousand, five hundred dollars for last year. Twenty-five percent, ninety thousand dollars is twenty thousand five hundred dollars. You get a big raise this year, big raise. We're going from ninety thousand last year to ninety thousand and one dollar. We got a one dollar raise, big raise. Many people think instead of paying twenty-five percent in taxes from last year, now that they're over the ninety thousand dollar limit, suddenly they're paying twenty-eight percent in taxes.

They say or they think, "Oh, I got a dollar raise. I'm going to pay a bunch more money in taxes." People think that twenty-eight percent, ninety thousand dollars and one is twenty-five thousand two hundred dollars. The thinking goes, "I got a one dollar raise, and my taxes went up to twenty-seven hundred dollars. I lost twenty-seven hundred dollars by making a dollar more." They would be wrong on both accounts.

Here are how the brackets work again for a single person, rounding numbers. Zero to ten thousand dollars, ten percent on that money. From ten thousand dollars to thirty-five thousand dollars, you pay fifteen percent on those dollars. Any taxable income above thirty-five thousand dollars, but less than ninety thousand dollars is taxed at the twenty-five percent rate. The dollars above ninety thousand up to a hundred ninety thousand dollars, are taxed at a twenty-eight percent rate.

Back to our example of ninety thousand and one dollars. I'm just going to rip through these numbers, because you're going to get glassy eyes anyways. The ten thousand dollars, zero to ten thousand dollars, is a thousand dollars on taxes on that. The ten thousand to thirty-five thousand dollars, that's, how much is that? Well, it's twenty-five thousand dollars, thirty-five minus ten. That's the range. Twenty-five thousand dollars times fifteen percent, because dollars are in that bracket, are tacked fifteen percent. That's three thousand, seven hundred fifty. Then the thirty-five to ninety, ninety minus thirty-five is fifty-five thousand dollars. There's fifty-five thousand dollars taxed at twenty-five percent, which comes out to thirteen thousand seven hundred fifty dollars.

All totaled up, it's eighteen thousand five hundred dollars, which is much different than if you took ninety thousand and multiplied it by twenty-five percent, which again was twenty-two thousand five hundred dollars. It's a three thousand dollars difference. What about that extra buck? That buck form that big raise we got? That extra dollar is taxed at twenty-eight percent, or twenty-eight cents.

A salary of ninety-thousand and one dollars puts you in the twenty-eight percent tax bracket instead of eighteen thousand five hundred dollars, which you'd owe if you'd made ninety thousand dollars, you now owe eighteen thousand five hundred dollars and twenty-eight cents. What does that really mean when somebody says, "Well, what tax bracket are you in," or, "I'm in the X percent tax bracket?"

Roughly speaking, it's the tax rate you pay on the highest dollars of your taxable income. It is not the tax rate you pay on all your income after you take out adjustments, deductions, and exemptions. It's not, "Okay, I'm in the twenty-five percent tax bracket. I pay twenty-five percent in taxes." If that were the case, we'd have what was called a flat tax. It would just be flat twenty-five percent across the board. Here in the United States, we have a progressive income tax system. That means the more money you make, yeah, your tax rates will go up, but only on those dollars earned within that range that, you shouldn't be concerned about entering a new, higher tax bracket. You always pay more taxes as you earn more money, if you go up in a tax bracket or not.

If you go from sixty thousand to sixty-five thousand dollars, pay more in taxes. Sixty-five thousand to seventy thousand dollars in income, you pay more in taxes. Eighty to ninety, you pay more in taxes. Hundred and thirty to hundred twenty, pay more in taxes. You will never be worse off earning more money like the lady at the beginning in the story thought she was, because the money you earn in the lower tax brackets is taxed at the exact same rate. Only the money at the highest tax bracket is taxed higher.

Let's build on our single person making ninety grand. Let's say, last year they earned ninety grand, and they're getting a twenty thousand dollar increase in salary and bonus next year. They're going from ninety to a hundred ten. Only that twenty thousand dollars is going to be taxed at twenty-eight percent. Only that twenty thousand dollars, because it's above the ninety thousand dollar range for that bracket. The whole hundred ten doesn't get taxed at twenty-eight percent, only the new twenty thousand dollars. Dollars thirty-five through ninety, taxed at twenty-five percent. Dollars ten thousand through thirty-five thousand dollars, taxed as fifteen percent still.

Dollars zero through ten thousand dollars still taxed at ten percent. None of that changed. That person get a twenty thousand range, a two ... I'm sorry, a twenty thousand dollar bonus, a two hundred thousand dollar increase in salary, a two million dollar increase in salary, dollars zero through ten percent still going to be taxed at ten percent. Dollars ten thousand through thirty-five thousand dollars, still taxed at fifteen percent. Dollars thirty-five thousand through ninety thousand, still taxed at twenty-five percent.

If you missed that, number one, go back and listen again. Number two, the easiest way to do this is to Google tax brackets for the current year. When you see it laid out with the dollar amounts and the percentages, it will become much more clear. You'll say, "Okay, I get it now." Tomorrow, we'll keep building on this. Tomorrow, we'll look at how knowing what your tax bracket is, and those different rates can help you save money.

"Dear Mr. Turner,

Thank you for your letter in reference to the order you placed for Mother's Day with 1800flowers.com. I would first like to apologize for the frustration you experienced with this issue. My brother Chris, our president and I take customer satisfaction very seriously. In our relentless, in our efforts to deliver smiles for our customers.

I apologize that we have disappointed you and your mother. Please be assured that this issue will be addressed immediately.

Sincerely,

Jim McCann, CEO, 1800flowers.com."

Personally signed by the CEO of 1800Flowers.com. If you missed a while back, I placed a order for flowers for mom which did not get delivered, and I didn't find out they didn't get delivered until several days after Mother's Day had passed. One of the things I emphasize on the show is always go to the top. Don't waste your time with customer no service, which 1-800-Flowers may have good customer service or not. I just, typically I don't even bother trying. No, actually I did spend twenty minutes on the phone with them. I forgot that a couple days after that.

I decided, "All right, I'm just going to ... I'm going to write a letter." Looked up the contact information for the CEO. I was polite. I stated, "Here's what happened. Here's how I'd like you to address the issue. i.e., I want some free flowers for mom, because you messed up my order." Mom got her free flowers. She called me. It took a while to get them. That's not ... Forget about that issue. She did not, obviously didn't get them on Mother's Day. She got an upgraded bouquet from what I had ordered. The executive assistant to the CEO left two voicemails for me. She called my mom as well. Emailed me a couple times saying, "Hey, we're going to resolve this issue." Followed up with me, and on top of that, a letter from the CEO.

This stuff works, nation. It works. That is proof positive right there. Who were the big winners and losers in this whole thing? Well, my mom won. I was a winner. I got what I had asked for out of it. Did 1-800-Flowers, were they a winner or a loser in this? They had to give up some free flowers. They got a customer for life. They did what smart business owners do. Business owners of good and successful companies. Companies that are well regarded in the industry. The exact opposite of what you can expect from somebody like a cable company or a cellphone company or many of the airline industries who are so concerned about nickeling and diming and losing money, that they would rather look at the dollars and cents instead of doing what is right for the customer, when in turn when you do what is right for the customer, you end up making more money in the long run.

They never see that. They're only looking at, "How am I going to make my quarterly reports, or quarterly numbers that I can get the bonus that I was promised?" When you deal with some of these craptastic companies that have these terrible customer service, that is what it boils down to, and that is what they're looking at. When you're dealing with some of these wonderful companies, like 1-800-Flowers, look at all the free advertising they're getting on this show because of what they did.

Just a couple takeaways, if you're a consumer, a customer, and you've got an issue, again go straight to the top. Don't make the phone call to the customer service. Write a letter to the CEO. Send it in the mail. That is much more likely to get your desired outcome. Number two, if you're a small business owner, stop worrying about the nickeling and the diming of your customers. Get the problem solved, and you'll have a customer for life. People over profit. When you choose people over profit, the profit ends up going up ninety-nine point nine percent of the time. Yes, one out a thousand are jerk customers. Fire them. Move on. Part of life. The ninety-nine point nine percent of the other good customers, they are going to make you your money. They are going to grow your business. They are going to spread the word. They are going to help you out.

That is free advertising that you would have to pay tens of thousands of dollars to get otherwise through traditional advertising avenues. Word of mouth matters, either positive or negative. Best if you're running a small business, you need to be on the positive end of it. Thank you 1-800-Flowers for taking care of mom.

Tammi gets an offer to be a virtual assistant. Is it legit? She says,

Tammi: "I am fifty-four years old. Really starting to pay attention to my finances, and working in the oil and gas industry has been rough during the last two years. We had two lay off rounds last year, and now we are facing another round that will occur coming up. After having worked in this industry for the past thirty plus years, I've never been laid off, but now I figure it may be my turn. I started seeking opportunities for multiple income streams so that I never have to be concerned about the possibility of losing my job. I have signed up with Upwork, submitted applications for jobs I feel I can perform between my job and other responsibilities.

"Recently a company has contacted me via email to perform virtual assistant responsibilities. So far I have not been able to find out if this is a legitimate company. The work sounds interesting, but I don't recall reaching out to them. How can I find out more about this company, and if they are for real before I submit paperwork with them? Below is the content of the email. Would really appreciate any feedback."

Here is the email Tammi included. It says, "Hello. You will receive a compensation of twenty-five hundred dollars to you upon completion. There is only one way to apply for this part time position. You have to sign up on the website, which is given. Once you sign up, you'll get access to our client area." Let's see what else here. "Once you complete this step, follow the instructions on the screen. We receiving a lot of application forms, and must arrange everything before you start. Usually it takes a day or two, so expect an email within the next few days with instructions on how to proceed."

Scott A. T.: Good for you, Tammi, for planning ahead. You've seen the writing on the wall, and are preparing for that. That's excellent on your behalf. You are right. Your spidey senses should be tingling, or your bat senses. Whatever superhero, your Wonder Woman senses. Whoever gives you your super senses, they should be tingling right now. This site, and I'm going to share the website with everybody, usa51.com. Usa51.com is the name of it. It makes me very, very nervous, just because if it sounds too good to be true, it's most likely too good to be true.

They say it's thirty-thousand dollars a year, twenty-five hundred bucks a month, plus 401k and health benefits. Work from home. Set your own hours. Sounds like a great deal. Are there virtual assistant positions out there like that? Oh yeah. Absolutely. It's just the presentation that these guys have put forth is what makes me nervous, and that they've reached out to you directly. You don't even know who they are. It's like they're stalking you. Maybe they're looking for potential targets we'll say on Upwork.com, and try to get people to sign up that way.

I took it upon myself to apply for a job. I actually, not me. It was my cat. I just want to see what's going to happen. I took an old resume, tweaked it a little bit, filled out the form, uploaded my resume, included a picture of my cat. Riker is going to be applying for one of these VA jobs, and we're just going to see what happens. After you do apply, you submit some, it wasn't a whole lot of personal information to get into the system. One of the first forms you're going to see within there is a W-4, which is going to require you to submit, what? Your Social Security number. I just have this feeling, kind of like you did, it's not legit. They're looking to get people in there with this bait of a well-paying job. Work from home. Get your personal information, Social Security number, and get into some type of identity theft scam operation.

I'm not saying they are. I'm not saying that. Whoops, dropped a couple books there. I'm not saying they are. That's just what it feels like. We're going to find out. I'll report back on rather Riker gets approved for this job, what kind of paperwork they're looking for, and we'll take it from there. For now, yes. I would stay away from it. Steer clear. Thanks for the question, Tammi. Good luck in your job hunt.

Shake, shake, shake. Back in two shakes of a lamb's tail. Hey, nation. Scott Alan Turner here. Now, for those of you that are my longtime listeners, all fourteen of you, you know I'm not one of those guys on the radio who promotes every product that shows up on their desk. If you're a new listener, well, I apologize on behalf of your friend who recommended you to listen to this garbage. At least the cat appearances are entertaining. Unless you're a dog person. Then it's just another reason to unsubscribe. The Tourism Board of Andorra invites you to visit this tiny, four hundred sixty-eight square kilometer, independent principality situated between France and Spain in the Pyrenees Mountains. It's known for its ski resorts and a tax haven status that encourages duty-free shopping. You can also experience a delicious casserole that tastes of the high mountains. I guess it either tastes like snow or dirt, depending on the time of year. Visit Andorra. Tell them Scott Alan Turner sent you.

Chris is forty-three and is wondering if he's behind on his retirement savings.

Chris: "We have eighty thousand dollars a year in income. Our mortgage is eight hundred dollars. We have car loans of six hundred dollars a month, and credit card debt totaling about seven thousand dollars. I'm a machinist and my wife works at a restaurant. We have fifty thousand dollars saved."

Scott A. T.: My dad, he also worked he also worked in a machine shop. He was painting taps and dies in his later years, and mamma worked at a coffee shop, so a little similarity there. They weren't earning anything near what you guys were, though. Fidelity guidelines, and these are just rough estimates for talking points, but for individuals by age forty should have two times your gross annual salary saved towards retirement. You're in your forties, early forties, eighty thousand income, you should have a hundred sixty thousand dollars socked away so far.

Again, that's a benchmark just for talking points. You're a bit behind that, but compared to your peers, you're a thousand percent ahead, because half of people in their forties have zero dollars saved, so you're way ahead of most people. Are you behind? Yes, no, maybe. It could be any of those. Until you have some clearer retirement goals, and your lovely bride agrees to them together, it's kind of like you're spinning around with a blindfold on, and you're trying to play pin the tail on the donkey. You don't know if the donkey is in front of you, behind you, on the side of you, or in a completely other state, or on an airplane flying over your head. You don't know.

The first goal is you guys have got to get that credit card debt gone, because you can't build wealth while you're paying off debt like that, significant wealth. Cut up the cards. Get on the cash budget. Have your written spending plan where you're spending your money before you get it each month. Get that debt knocked out. That's going to put you on the accelerated path to building a ton of wealth and having a wicked comfortable retirement. You've got to have a goal for your money each month.

Eighty thousand dollars in income, you guys really don't have that much debt when I'm looking at those numbers. If you love your cars, and they're almost paid off, you can keep them. If not, you've got a lot of debt on those cars, and you're going to keep paying that. That's money that could go towards your retirement, which you're just throwing away each month on those car payments. If I'm in your shoes, I'm probably going to get rid of one of those cars, depending on what the loan balance is. If it's significant, yeah I'm definitely going to unload it, because that's a key wealth builder, not having a car payment where you can divert that towards investments. Plus you accelerate your savings real quick.

Your mortgage, it's pretty tiny relative to your income. Keep that up with the modest housing. I wouldn't upgrade your living quarters anytime soon. That low month mortgage, that is going to help you build more wealth. You've got to make sure you've got your three to six month emergency fund in place in case you have an unforeseen circumstance where you have a loss of income. Then you go to start socking away for your retirement. After that, start throwing extra money on the house if you want to get that paid off sooner. First, you've got to figure out your retirement plans on paper. "When are we going to retire? What age are we thinking of retiring?" Both you and your wife, "What is our retirement going to look like? Are we going to travel the world? Are we going to just continue to live in our modest house and sit on the front porch hanging out with the grandkids?" Which takes a lot less money than traveling the world.

You're on your way to a comfortable retirement if you get these debts gone and start throwing more money at your retirement. I ran some numbers for you on the calculator on scottalanturner.com, my investment calculator. Fifty thousand dollars a month, which is where you are right now, if you start putting away fifteen percent of your income, after you get the debts paid off, after you get a thirty-six month emergency fund in place, that's a thousand dollars a month that you can put towards your retirement savings.

in twenty years, just earning ten percent, you're going to have one point one million dollars. I'm going to repeat that, because that's pretty cool. Fifty thousand now, fifteen percent of your income, which is a thousand dollars a month in retirement, in smart investing, twenty years at ten percent, you're going to have one point one million dollars. Now, I don't want to rain on your parade. One point one million dollars twenty years from now doesn't buy what one point one million dollars can today. Maybe in twenty years, that might not even be enough, depending on what you want your retirement to look like. That's why you might want to consider putting away twenty percent of your income.

Again, that's just a number. It depends if you want to retire at fifty-five, that number's got to be a lot bigger. If you want to retire at age seventy, then you've got some more flexibility in that. If you live a very frugal lifestyle, you're not going to spend each month. You're getting the early bird special at the restaurant each day, spending five, six bucks a piece on dinner, that's a lot different than you want to eat steak and lobster every night. You've gotta go figure out those things ahead of time, figure out what you're retirement's going to cost you, figure out where you are now, and what the gap is you need to make up in order to sock that money away.

The way you can do that and get much more clarity is by sitting down with a fee only certified financial planner, who will charge you for a couple hours of their time, run some numbers based on your specific situation. Some of them charge flat fees as well. They'll give you a good idea of a plan that you need to follow in order to get you from point A to retirement in point business, with your salary, your savings, and your retirement goals. You can find them on the garrettplanningnetwork.com, or xyplanning.com is another service where they have fee only certified financial planners. Those links will be in the show notes. Thank you, Chris, for the question.

Pat in Hawaii asks if 457(b) or 403(b) plans are better.

Pat: "I teach in Hawaii, and the 403(b) seems to be like most, and sucks. I cannot find any prospectus or expense ratios. It looks like a bunch of annuities, and a lot of the providers have a bad reputation. There's a 457(b) Island Savings Plan that seems decent. It has some low cost index funds, but I'm no expert. Could you look at these and tell me your expert opinion? Also, what are the pros and cons of a 457(b) versus a 403(b)?"

Scott A. T.: With both those plans, you can make tax-deferred contributions, so they're taxed upon distribution in your retirement. A 403(b) plan generally more common, and it's easier to transfer to a rollover IRA after you retire, or leave your job. 457 plans can be a little more restrictive, depending on if your employer is a government or a nonprofit employer like a hospital. If you're working for a school, you're working for the government, not going to be an issue for you. Why does the rollover matter? If you're picking between those, well if you get the opportunity to rollover them later after you've retired or you leave your position, you get more options in your brokerage or wherever you rollover to to pick from.

If you don't have that option, you get stuck with whatever's in the plan. You are correct. The choices in the 4013(b) are mostly annuities. Let's see. I wrote down the number here. Where did it go? Twenty-seven out of your thirty-four choices in that plan are annuities. You only get seven choices of mutual fund companies or options to pick from.

What's wrong with annuities? They get tax deferred, right? That's what we want. Well, because of the plan, 403(b), it's already tax-deferred. Putting an annuity in a plan that's already tax-deferred, it's like wearing a raincoat inside. It's useless. People get sold on a benefit that the code already provides. The worst thing is the massive, massive fees which can range from two to five percent. Hundreds of percents higher than what you can get on a low cost index fund, a low cost mutual fund. I'm going to give you an example coming up, which you may or may not know why fees matter.

If you are with a 403(b) plan run by TIAA-CREF, they are cream of the crop. Pretty much one of the very, very, very few good nonprofit providers of 403(b) plan. They're like the Vanguard of the 403(b) world. Very low cost options to pick from. If it's me, if I'm in your shoes, first thing I'm considering is expenses. The second thing I'm considering is expenses, and the third thing I'm considering are expenses. That's all I'm looking to do. I want to max out my retirement, and make as much money as I possibly can. Get my money compounding early and often so that I have more in retirement.

I don't care about loans. If I can pull out a loan. I don't care about early withdrawals or any of those extra things, add-ons that different plans have. I want maximum money. That is all I care about. To get that, I've got to have proper asset allocation, low cost funds to invest in. That's kind of it. From what you've got, it's kind of a no brainer. The 403(b) plan is a bunch of annuities, and a few mutual funds I picked from, high fees.

What about the Island ... What do we call it here? The 457(b) Island Plan. Couple choices in there. You've got a Life-Cycle Fund. That's a target date fund, where they, it's a fund of funds, where they do the asset allocation for you. You pick the year that you wanted to retire in. Make up a number. 2040, if that's the year you want to retire, and they adjust the asset allocation as you approach that date. Moving from more stocks into less stocks, more conservative as you approach your retirement date.

The funds that you have access when doing that plan have an expense ratio of zero point six one percent. Not terrible, not great. What can we do instead? You've got access to four very, very, very, very, very, very, very good index funds in that plan. You've got a BlackRock US Small Midcap Index. That's point zero seven percent. That's a total stock market index, buying a piece of every stock that's out there. That's a very low expense. You've got a non-US equity index. That's all the international stuff. That's gotta expense ratio of point one one percent. Again, very low. Compare that to the point six one percent of the Life-Cycle Fund. You get a bond index and a large cap index, both from BlackRock, point zero seven percent.

Those are the four index funds that you can pick from. I ran a quick calculation on the website 401kfee.com. You can plug in some numbers. I picked eight percent as a return. That's very conservative. I plugged in two numbers for fees. I put in the point six one percent for your Life-Cycle Fund. Then I put in point zero seven percent if you went with some of those index funds, just as an average. I said, "Hey, let's start with a hundred bucks. Let's contribute nine thousand dollars a year to the plan. Let's pretend we're forty, and we're retiring at age sixty-five. What's that going to pull it out for us?" Well, we're going to save fifty grand if we go with the index funds over the Life-Cycle Fund. You could retire a year early with that extra fifty grand by making that choice.

You can plugin with your own numbers on that calculator based on what you're contributing, when you plan on retiring. You can use the Life-Cycle Fund as a guide. Dig into that perspective. Some will say, "All right, we've got this percent in the total stock market index, and we've got this percent over here in international." It's got like, I want to say eight or ten or twelve funds within that one Life-Cycle Fund. Whereas if you go with these index funds, the BlackRock ones, you've got to do your own asset allocation. You're going to have to say, "All right, I'm going to put X percent in the total stock market, and I'm going to put," make up a number, "Sixty percent, and I'm going to put twenty percent in the bond index, and then I'm going to put twenty percent in the international."

You'd have three index funds that you'd pick that covers pretty much everything in the stock market. You'd have a three fund portfolio. You're basing your asset allocation on what is in the Life-Cycle Fund using that as a point of reference. You can do that on your own, if you're comfortable with it, or you go out and you pay a fee-only certified financial planner for a couple hours of their time, and say, "Here's my options. Do the asset allocation for me." Is it worth the couple, three, four, how ever many hundreds of dollars it's going to cost you for them to save you ten, twenty, thirty, forty, fifty thousand dollars years from now? You bet you. You bet you it does, because fees matter. Thanks, Pat, for the question.

In 1626, Native Americans sold what is now called Manhattan Island, New York, to settlers for a pile of trinkets worth about twenty-four dollars. Manhattan's value as a real estate today is appraised at twenty-four billion dollars. If the Native Americans had sold those trinkets for twenty-four dollars cash, and placed the money in a six percent compound interest account, their investment today would be worth twenty-seven billion dollars. If today's Native Americans had inherited that fortune, they could buy back Manhattan and have three billion dollars leftover.

It's not to say the Native Americans didn't get a fair deal, but rather to illustrate that what seems like might be a small amount, twenty-four dollars in trinkets, might be a lot more than you thought, or have a lot more potential. In other words, great accomplishments don't necessarily require a huge initial investment, or the talent of genius, or an incredible windfall, or superhuman efforts. Great accomplishments are possible for anyone who can muster just a little bit, and then keep at it with persistence. That story is from Tax Free Retirement by Patrick Kelly.

Those are the words. That's it for this episode. I'm your host, Scott Alan Turner. Rock Star Katie's my producer. All the links mentioned in this show are available in the show notes. Scottalanturner.com. If you have a question you'd like answered on the show, please visit goaskscott.com. Thank you for listening.