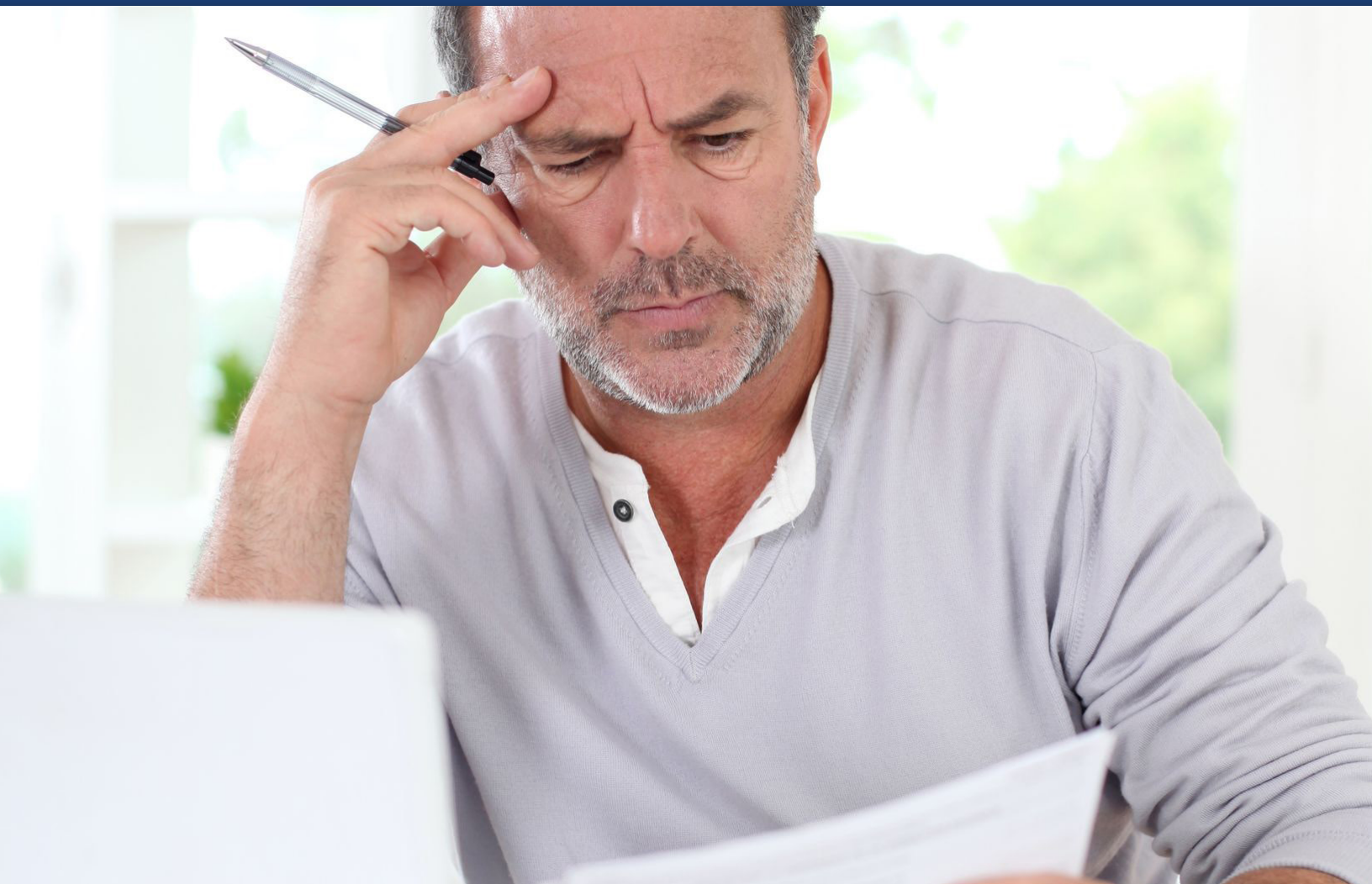


The Shocking Truth About Taxes & Retirement

CALCULATING THE IMPACT OF REQUIRED MINIMUM DISTRIBUTIONS



Who Says You Have to Spend Your IRA? ...Oh Yeah, Uncle Sam

Brought to you by
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HYDER

UNCLE SAM SAYS: YOU MUST SPEND YOUR IRA

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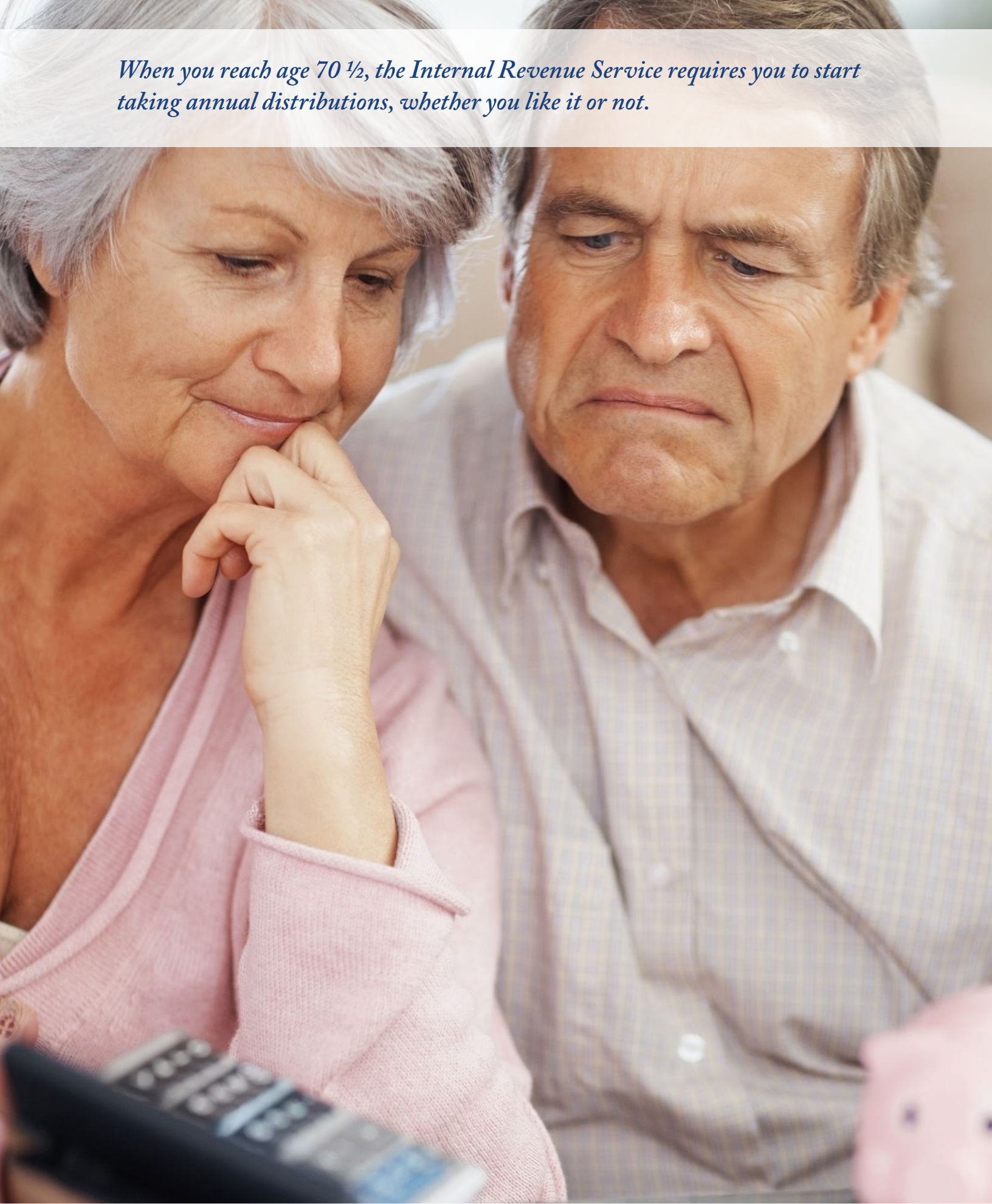
If like millions of Americans you've invested your hard-earned retirement savings into IRAs or employer-sponsored retirement plans (such as 401(k)s, 403(b)s, or 457 plans), be prepared. When you reach age 70 ½, the Internal Revenue Service requires you to start taking annual distributions, whether you like it or not. These mandatory withdrawals are called required minimum distributions, or RMDs, and the tax impact is significant.

Why RMDs and How Do They Work?

As you are most likely aware, any money invested in these tax favored retirement vehicles receives the benefit of tax-deferred growth throughout your working years, allowing you to accumulate more money faster, by not taxing the growth along the way. However, this also means that Uncle Sam receives no tax revenue on the growth

and contributions until you take a withdrawal. Therefore, in order to ensure you do take withdrawals from your retirement accounts, the IRS came up with the concept of a Required Minimum Distribution, forcing you to take withdrawals from your qualified retirement plans by imposing significant penalties on anyone who doesn't.

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When Do RMDs Begin?

Your first required minimum distribution must be taken by April 1st of the year following the year that you reach age 70 ½. RMDs for each

subsequent year must be withdrawn by Dec. 31st of that particular year. Confused? Let's look at the following example for clarification.

John Smith, Age 70:

- ››› *John turns 70 on Jan. 15, 2012. This means he turns 70 ½ on June 15, 2012, so he must take his 2012 required minimum distribution by April 1, 2013, at the latest.*
- ››› *He also has to take a 2013 required minimum distribution, but that doesn't need to be taken until Dec. 31, 2013. This is also the case for all subsequent years.*
- ››› *So, for example, John's 2014 required minimum distribution needs to be taken by Dec. 31, 2014, and so on.*
- ››› *To avoid paying taxes on both withdrawals in 2013, John can take his 2012 required minimum distribution by Dec. 31, 2012, and he would have to pay tax only on that withdrawal for the 2012 tax year and then only have to pay taxes on the required Dec. 31, 2013, withdrawal for the 2013 tax year.*

Potential Ramifications:

Do RMDs cause unexpected consequences for some retirees? Absolutely! Below are a few considerations:

››› Income:

If you're like many retirees, you may not need your IRA for income at age 70 ½, but regardless the IRS says you have to take a distribution each year. Before you reach age 70 ½, work with an advisor to determine what impact, if any, this extra income may have on your Social Security benefits.

››› Annual Taxes:

Taking RMDs creates additional tax bills each year, so make sure your tax preparer is informed of the amount(s) of the required minimum distributions you have to take. The amount of the taxes owed will be based on your income tax rate the year the required distribution is taken.

››› Accumulated Tax Burden:

Like most people you may realize that at some point you will eventually have to pay taxes on your IRAs and other qualified retirement accounts, but what you may not take the time to consider is how much these taxes will ultimately add up to. In many cases, your qualified retirement accounts may represent the largest tax bill you'll ever receive.

Since most people never take the time to assess the long term tax impact of these distributions, let's take a look at the following hypothetical example...

JOHN & MARY SMITH

The Story of John & Mary

Both John and Mary are currently 65 years old and have accumulated \$500,000 in John's IRA. They are currently taking no income from the IRA and are averaging a 6% return each year. As you can see, until age 70 ½ they

sail along smoothly, compounding the growth in the account. While they feel great about their growing balance, what they don't realize is that they are also compounding their future tax liability.

IRA Distribution Projections - Current

Year	Age Beg	Age End	Beginning Balance	6.00% Earning	RMD Divisor	Required Distribution	Actual Distribution	Less Tax 25.00%	Net Distribution	Net of Tax	Net Reinvested	Ending Balance
2008	64	65	\$500,000	\$30,000	0.0	\$0	\$0	\$0	\$0	\$0	\$0	\$530,000
2009	65	66	\$530,000	\$31,800	0.0	\$0	\$0	\$0	\$0	\$0	\$0	\$561,800
2010	66	67	\$561,800	\$33,708	0.0	\$0	\$0	\$0	\$0	\$0	\$0	\$595,508
2011	67	68	\$595,508	\$35,730	0.0	\$0	\$0	\$0	\$0	\$0	\$0	\$631,238
2012	68	69	\$631,238	\$40,147	0.0	\$0	\$0	\$0	\$0	\$0	\$0	\$669,113
2013	69	70	\$669,113	\$40,147	27.4	\$24,420	\$24,420	\$6,105	\$18,315	\$0	\$18,315	\$684,839
2014	70	71	\$684,839	\$41,090	26.5	\$25,843	\$25,843	\$6,461	\$19,382	\$0	\$19,382	\$700,087
2015	71	72	\$700,087	\$42,005	25.6	\$27,347	\$27,347	\$6,837	\$20,510	\$0	\$20,510	\$714,745
2016	72	73	\$714,745	\$42,885	24.7	\$28,937	\$28,937	\$7,234	\$21,703	\$0	\$21,703	\$728,692
2017	73	74	\$728,692	\$43,772	23.8	\$30,617	\$30,617	\$7,654	\$22,963	\$0	\$22,963	\$741,797
2018	74	75	\$741,797	\$44,508	22.9	\$32,393	\$32,393	\$8,098	\$24,295	\$0	\$24,295	\$753,912
2019	75	76	\$753,912	\$45,235	22.0	\$34,269	\$34,269	\$8,567	\$25,702	\$0	\$25,702	\$764,878
2020	76	77	\$764,878	\$45,893	21.2	\$36,079	\$36,079	\$9,020	\$27,059	\$0	\$27,059	\$774,691
2021	77	78	\$774,691	\$46,481	20.3	\$38,162	\$38,162	\$9,541	\$28,622	\$0	\$28,662	\$783,010
2022	78	79	\$783,010	\$46,981	19.5	\$40,154	\$40,154	\$10,039	\$30,116	\$0	\$30,116	\$789,837
2023	79	80	\$789,837	\$47,390	18.7	\$42,237	\$42,237	\$10,559	\$31,678	\$0	\$31,678	\$794,990
2024	80	81	\$794,990	\$47,699	17.9	\$44,413	\$44,413	\$11,103	\$33,310	\$0	\$33,310	\$798,276
2025	81	82	\$798,276	\$47,897	17.1	\$46,683	\$46,683	\$11,671	\$35,012	\$0	\$35,012	\$799,490
2026	82	83	\$799,490	\$47,969	16.3	\$49,048	\$49,048	\$12,262	\$36,786	\$0	\$36,786	\$798,411
2027	83	84	\$798,411	\$47,905	15.5	\$51,510	\$51,510	\$12,878	\$38,633	\$0	\$38,633	\$794,805
2028	84	85	\$794,805	\$47,688	14.8	\$53,703	\$53,703	\$13,426	\$40,277	\$0	\$40,277	\$788,790
2029	85	85	\$788,790	\$47,327	14.1	\$55,943	\$55,943	\$13,986	\$41,957	\$0	\$41,957	\$780,175
2030	86	87	\$780,175	\$46,811	13.4	\$58,222	\$58,222	\$14,556	\$43,667	\$0	\$43,667	\$768,764
2031	87	88	\$768,764	\$46,126	12.7	\$60,533	\$60,533	\$15,133	\$45,399	\$0	\$45,399	\$754,357
2032	88	89	\$754,357	\$45,261	12.0	\$62,863	\$62,863	\$15,716	\$47,147	\$0	\$47,147	\$736,755
2033	89	90	\$736,755	\$44,205	11.4	\$64,628	\$64,628	\$16,157	\$48,471	\$0	\$48,471	\$716,333
TOTALS:						\$908,005	\$908,005	\$227,001	\$681,003	\$0	\$681,003	

Hypothetical only - no specific investment illustrated.



At age 70 ½ you can see that John's first RMD is due to be taken. In that year his IRA has an accumulated value of \$669,113. Therefore his RMD that must be taken is \$24,420 (His balance divided by the "RMD Divisor").

What John and Mary weren't expecting was the tax bill this creates which in this year, given their 25% tax bracket is a staggering \$6,105. Ouch! What John and Mary are most upset about however is the fact that this scenario will now play out every year for the rest of their lives, only the amount they will be required to withdraw will increase with each passing year, compounding the amount of taxes owed.

If we fast forward to their age 90, which statistically one of them will most likely live to, you can see that the total distributions they will have been forced to take will be \$908,005, and the total taxes owed on that \$908,005, is a staggering \$227,001! That's over a quarter of a million dollars that goes straight to Uncle Sam. But it gets worse...

At the end of John & Mary's lives, they pass on the remainder of the IRA balance to their children, which you can see in the bottom right

column is \$716,333. Now, when their children inherit this money, guess who shows up at their door to collect their share. That's right, Uncle Sam again. The amount of the inherited IRA will be added to their children's earned income for the year, likely placing them in a higher tax bracket and again a significant portion of the inherited IRA going to taxes.

In Summary, John and Mary were forced to withdraw and were taxed on over \$900,000 dollars, while their children were taxed on the remaining \$700,000 dollars they inherited, meaning the total amount they and their family were taxed on was \$1.6 million dollars! Creating a total tax bill in excess of \$400,000 dollars between them and their children.

Considering their IRA is worth only \$500,000 dollars today, that's a significant tax burden. You see the opportunity you have is not necessarily to shelter the money you have already accumulated in your IRAs and other retirement plans, but it's the future growth that you can protect from taxes. Let's look at another hypothetical scenario in which John and Mary convert their \$500,000 dollar IRA and reposition it to a Roth IRA to assess the potential tax savings.

John & Mary Convert to a Roth IRA

In the example below we can see that John and Mary start with the same balance of \$500,000 but in this case they decide to convert their IRA over a ten-year period. They do this to keep from jumping in to the next tax bracket.

Even though they are not required to take distributions yet, they elect to begin converting their IRA starting right away at age 65. Each year for ten years they convert \$67,934, which creates a tax bill of \$16,983, which they pay out of the IRA distribution. The net effect over the ten-year period was total taxable distributions of \$679,340 for a total tax bill of \$169,835. The good news for John and Mary however is that they are now done paying taxes on this account, forever. They went from taxable distributions of \$1.6 million to just \$679,000, thus reducing the amount they owe taxes on by almost \$1 million dollars!

And, the money that their beneficiaries will receive at their death is now tax-free!

While this scenario considers a number of variables, all of which are different for every client we work with I hope that your eyes have been opened to both the potential tax liability hiding in your IRAs and qualified accounts as well as the opportunity you have to do something about it. As a general rule, the sooner you begin the conversion process the more you stand to gain. Please do not take action on this strategy without first consulting with a professional. If you would like to see an analysis similar to John and Mary's please schedule a free strategy session and let us run some preliminary analysis and projections for you. It just might be the most impactful thing you could do to reduce your future tax liability, both for you and your beneficiaries.

IRA Distribution Projections - Potential Rollout

Year	Age Beg	Age End	Beginning Balance	6.00% Earning	RMD Divisor	Required Distribution	Actual Distribution	Less Tax 25.00%	Net Distribution	Net of Tax	Net Reinvested	Ending Balance
2008	64	65	\$500,000	\$30,000	0.0	\$0	\$67,934	\$16,983	\$50,950	\$0	\$50,950	\$462,066
2009	65	66	\$462,066	\$27,724	0.0	\$0	\$67,934	\$16,983	\$50,950	\$0	\$50,950	\$421,856
2010	66	67	\$421,856	\$25,311	0.0	\$0	\$67,934	\$16,983	\$50,950	\$0	\$50,950	\$379,233
2011	67	68	\$379,233	\$22,754	0.0	\$0	\$67,934	\$16,983	\$50,950	\$0	\$50,950	\$334,053
2012	68	69	\$334,053	\$20,043	0.0	\$0	\$67,934	\$16,983	\$50,950	\$0	\$50,950	\$286,163
2013	69	70	\$286,163	\$17,170	27.4	\$10,444	\$67,934	\$16,983	\$50,950	\$0	\$50,950	\$235,398
2014	70	71	\$235,398	\$14,124	26.5	\$8,883	\$67,934	\$16,983	\$50,950	\$0	\$50,950	\$181,588
2015	71	72	\$181,588	\$10,895	25.6	\$7,093	\$67,934	\$16,983	\$50,950	\$0	\$50,950	\$124,550
2016	72	73	\$124,550	\$7,473	24.7	\$5,042	\$67,934	\$16,983	\$50,950	\$0	\$50,950	\$64,089
2017	73	74	\$64,089	\$3,845	23.8	\$2,693	\$67,934	\$16,983	\$50,950	\$0	\$50,950	\$0
TOTALS:						\$34,155	\$679,340	\$169,835	\$509,505	\$0	\$509,505	

Hypothetical only - no specific investment illustrated.

FREQUENTLY ASKED QUESTIONS

Q: What is the penalty if a required minimum distribution isn't taken?

A: To ensure you take your minimum distribution each year, the IRS assesses a hefty 50 percent penalty on the amount of the distribution that was not taken in time. Therefore, if your RMD is \$10,000 and you do not take it, you will be hit with a penalty in the amount of \$5,000! That's in addition to the tax owed on the distribution itself.

Q: If I own multiple IRAs do I have to take a required distribution from each?

A: If you own more than one IRA or qualified retirement account, the total required minimum distribution each year has to be calculated individually for each account but then can be withdrawn from one or more of the accounts as you wish. So long as the total amount of your required distributions for the year are withdrawn.

Q: How do you calculate an RMD?

A: You can calculate the RMD yourself but the trustee, custodian, or issuer who holds your IRA at the end of the preceding year must also either report the amount of the RMD to you, or offer to calculate it for you. To calculate your RMD, you will need:

1. The adjusted market value of your IRAs as of Dec. 31 of the prior year; and
2. The IRS table published in IRS Publication 590 that applies to your situation.

You will then calculate your required minimum distribution amount by dividing the prior Dec. 31 value of the IRA by the life expectancy factor determined by the appropriate IRS life expectancy table.

Q: Can more than the required minimum distribution be taken?

A: Yes, but you can't apply amounts in excess of the required minimum distribution to subsequent years' RMDs.

Q: What are the Publication 590 table options?

A: There are three defined tables in Publication 590 that you must pick from:

1. Uniform Lifetime Table III is to be used by:

- >>> Unmarried owners
- >>> Married owners whose spouses are not more than 10 years younger
- >>> Married owners whose spouses are not the sole beneficiaries of their IRAs

2. Life Expectancy Table II (Joint Life and Last Survivor Expectancy) is to be used by owners whose spouses are more than 10 years younger and are the sole beneficiaries of their IRAs

3. Life Expectancy Table I (Single Life Expectancy) is to be used by the beneficiary of an IRA

For Example... Let's say John is now 75 years old and is a widower, he would use the Uniform Lifetime Table III, which shows a distribution factor of 22.9. If his IRA was worth \$200,000 at the end of last year, he would need to withdraw \$8,734, which is calculated by dividing \$200,000 by 22.9.

Whatever you do, don't wait until it's too late! Taking action today could literally save you tens of thousands of dollars throughout your retirement!



IN SUMMARY

IRAs and other work-related investment accounts such as 401(k)s have been the most popular retirement savings vehicles for the past 30 years. However few people ever take the time to consider the long-term tax impact of these accounts and the required distributions that must be taken. One way to

avoid RMDs is to consider converting these accounts into Roth IRAs. This may or may not be a good option for you depending on several factors including; your age, the size of your IRAs, the amount of income you needed each year for living expenses, as well as your current income tax situation.

To determine if a Roth conversion would be a beneficial planning option for you, contact us to see what can be done to reduce the tax impact of your IRAs when your required minimum distributions start. Whatever you do, don't wait until it's too late! Taking action today could literally save you tens of thousands of dollars throughout your retirement!



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