What happens when 401(k) or IRA plans don't work as intended?

A life insurance strategy to help manage your retirement

The conversation

Traditional 401(k) and IRA plans are built around the concept of making pre-tax or deductible contributions and enjoying tax deferred growth. The tax benefits of that strategy work when tax rates are higher at the time you make the contribution than when you take the money out. However, after years of historically low tax rates and significant pressure for future tax rate increases, this formula may be turned upside-down! It's entirely possible that withdrawals from your 401(k) or IRA plans will be subject to higher taxes. If this is the case for you, it's time to get creative.

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The problem

The maximum marginal tax rates have recently risen, and alternative minimum taxes are affecting Middle America more than ever. In fact, the top federal income tax bracket has been greater than the current rate for 63 of the last 101 years.[1] This leaves many concerned that rising tax rates will reduce their retirement savings and income when they need it most.

When considering retirement income sources and assuming tax rates will continue to rise, one key challenge is structuring an investment portfolio that minimizes large tax bills during retirement years. Consider this: generally speaking, every dollar that goes toward retirement goes through three phases: contribution, accumulation and distribution. In a successful investment strategy, fund values grow in each phase (Chart A).

With regard to the taxes on your retirement savings during each of these three phases, there is good news and bad news:

- The bad news is that you must pay taxes on at least one of these three phases.
- The good news is that the IRS allows you to choose which phase will be taxed.

Ask yourself: 'Which phase would I rather pay taxes on?'

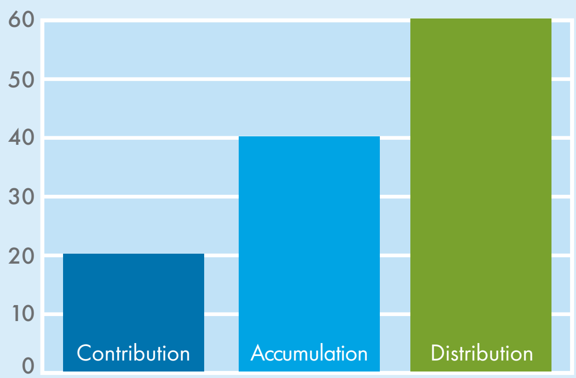
It's likely your answer will be: 'The lowest dollar figure!'

Often retirement portfolios consist primarily of qualified plans such as a 401(k) or IRAs, which incur taxes on the largest amount: distribution (Chart B).

With rising tax-rate pressure, this could be detrimental to traditional retirement plan assets. There are only a few options available where you pay no tax on the accumulation or distribution. Let's look more closely at one popular plan, the Roth IRA (Chart C).

Unfortunately, if your modified adjusted gross income is over $127,000 for single taxpayers or over $188,000 for married filing jointly (in 2013) you are not eligible to contribute to a Roth IRA. If you are under those income limits in 2013, you can only contribute a maximum of $5,500 ($6,500 if you are age 50 or over), indexed for future inflation.

Chart A: Retirement Income Sources



Investment losses can occur in the accumulation and distribution phases.

Chart B: Tax Payment Schedule

	CONTRIBUTION	ACCUMULATION	DISTRIBUTION
TRADITIONAL QUALIFIED PLAN/ IRA TAX TREATMENT	Non-taxable/ Deductible	Tax-deferred	Taxable
YOUR DESIRED TAX TREATMENT	Taxable/ Non-deductible	Tax-deferred	Tax-free

- So what can you do if you earn too much to contribute, or the amounts you can contribute are simply not enough to meet your needs?
- You may be concerned about tax payments on your retirement income. How can you save more for retirement and address these concerns?

Wouldn't it make sense to position a portion of your retirement assets to add death benefits and tax diversification to your portfolio?

Pay taxes now, and don't pay taxes in the future!*

The solution

With life insurance, you can add needed death benefit protection and tax diversification to a retirement portfolio.[2]

- Income-tax-free death benefit for your beneficiaries[3]
- No defined annual IRS limitation on premiums*
- No limit on gross income affecting your ability to contribute premiums
- Missed premiums may be 'made up' at a later time*
- Tax-deferred accumulation*
- Distributions using loans and withdrawals are income-tax-free when structured properly*
- No 10% penalty tax for accessing policy cash values prior to age 59 1/2 when structured properly*
- Take distributions as needed*
- No required minimum distributions (RMDs) for owners
- Self-completing upon death (death benefit exceeds account value)

Chart C: Roth IRAs Pros and Cons

PROS	CONS
• Accumulates tax-deferred • No taxes on qualified distributions • No RMDs for Roth-IRA owners • Income-tax-free inheritance to beneficiaries	• Non-deductible contributions • Limited amount you can contribute per year • Cannot make up missed contributions • If your income is too high you cannot contribute • Tax penalty may apply to withdrawals before 59½ • RMDs for Roth IRA beneficiaries • No death benefit for "self-completing"

Key benefits

Including life insurance as part of a retirement planning strategy has many advantages. For example, life insurance funded retirement strategies are self-completing in the event of death. The income-tax-free death benefit[3] will be paid to your beneficiaries if you die before funding is completed. In addition, there are no defined IRS-imposed annual limits on premium amounts and no income limits or contribution phase-outs like there are with Roth IRAs. Additionally, with the life insurance component of your retirement plan, you can skip or reduce premium payments at any time, and then potentially 'make up' those premiums at a later date.[4] In addition to tax diversification, this strategy provides you with additional life insurance. If you need more coverage, this meets your need and gives you tax diversification.

'Where are YOUR retirement assets being taxed?'

* Policy must comply with IRS requirements to qualify as a life insurance contract. Total premiums in the policy cannot exceed funding limitations under IRC 7702. Withdrawals during the first 15 years of the contract may be treated as income first and includible in policyholder's income. If the policy is classified as a modified endowment contract (see IRC 7702A), withdrawals or loans are subject to regular income tax and an additional 10% tax penalty may apply if taken prior to age 59 ½. Distributions will reduce policy values and may reduce benefits. Availability of policy loans and withdrawals depend on multiple factors including but not limited to policy terms and conditions, performance, and fees or expenses.

1 Tax Foundation: Federal Individual Income Tax Rates History. Nominal Dollars. Income Years 1913-2013

2 Clients need to be insurable and able to meet premium payments.

3 Life insurance death benefits are generally tax-free for beneficiaries under IRC 101(a), but may under certain situations be taxable in part or whole.

4 Subject to restrictions on your life insurance policy.

Find out how life insurance can help you plan for retirement

Learn more

Speak to your American General representative or visit **RetireStronger.com**.

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