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Stewardship Emphasis

A lifetime of hard work, a lifetime of prudent planning and management, and a strategy for enjoying the fruit of your labor is a solid formula for putting the gold in the golden years.

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Harvesting Retirement Income - Part 3

The last issue of The Empowerment Channel began the discussion of using retirement plans as income vehicles, mainly reviewing the types of vehicles and basic income tax issues with retirement plans. Now we will go deeper into the strategic aspects of retirement plan distributions.

Retirement Plans – The Cornerstone of Retirement Income Strategies (cont.)

As an income-producing vehicle, retirement plans as a group can provide you with a number of options for how you can receive the income. Depending on the vehicle you are using you may be able to choose from taking withdrawals on an as-needed basis, systematic withdrawals for a given period of time, annuitization (lifetime payments), or annuitization with specified minimum periods. Depending on the product from which you are taking income, you may be subject to redemption fees, and as we discussed in the previous issue, when income is distributed, you will incur tax consequences (unless using a Roth IRA). One of the arguments often made in criticism of some retirement plans is that on distributions you pay ordinary income tax at your highest marginal income tax rate, which may be higher than the capital gains tax rate (maximum 15%) that would be owed on a taxable investment. While there is truth to the argument, the fact is until your adjusted gross income (AGI) exceeds \$89,500 (for married filing jointly) or \$44,750 (for single), your total federal income tax would be no more than 15% of your AGI anyway.

It is good to know that you have a number of ways to receive retirement income, but perhaps a more important question is will you have enough of an asset base from which to draw your needed income? A number of factors go into that determination, but a critical issue for retirees is how will they continue to invest their available assets once they are no longer in an accumulation mode (i.e. making investment contributions). Conventional wisdom has always been to scale back on the amount of risk in your investments as you get older because you have a shorter time horizon, but the hard question has always been how much to scale back. This is especially true now that people are retiring earlier and living longer, meaning there is a longer investment distribution phase. In order to address that need, many investment companies now offer products that can provide investors with a greater level of comfort while investing in the stock market, allowing the investor access to greater potential returns with greatly reduced downside potential. These investments do come at a small price, but for the reduction of risk, many investors find it well worth the price and use these investments as an important part of a retirement income distribution plan.

Another scenario to consider is that you may only need minimal, if any, distributions from your retirement plan. In that case the plan could become a vehicle for transferring assets upon your death. Although your named beneficiary is the rightful heir to the money, both you and they face some unfavorable tax consequences. If the assets pass to your beneficiaries, they face the same situation as you would in terms of having to pay ordinary income tax on all of or a portion of the income. If the assets were in a taxable investment, the beneficiary would benefit from the IRS rule which values inherited assets received as of the date of death, so that is one drawback in using retirement plans as a way of transferring assets. The other drawback is that if you die as owner of the assets, they are subject to estate tax, which could significantly reduce the value of your estate. Despite these issues, retirement plans are a great way to gather assets for retirement income and give you options to do more advanced planning.

For the final issue of this series, we will review the use of life insurance in retirement income planning, which among other things addresses the estate tax dilemma of the retirement plan.



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