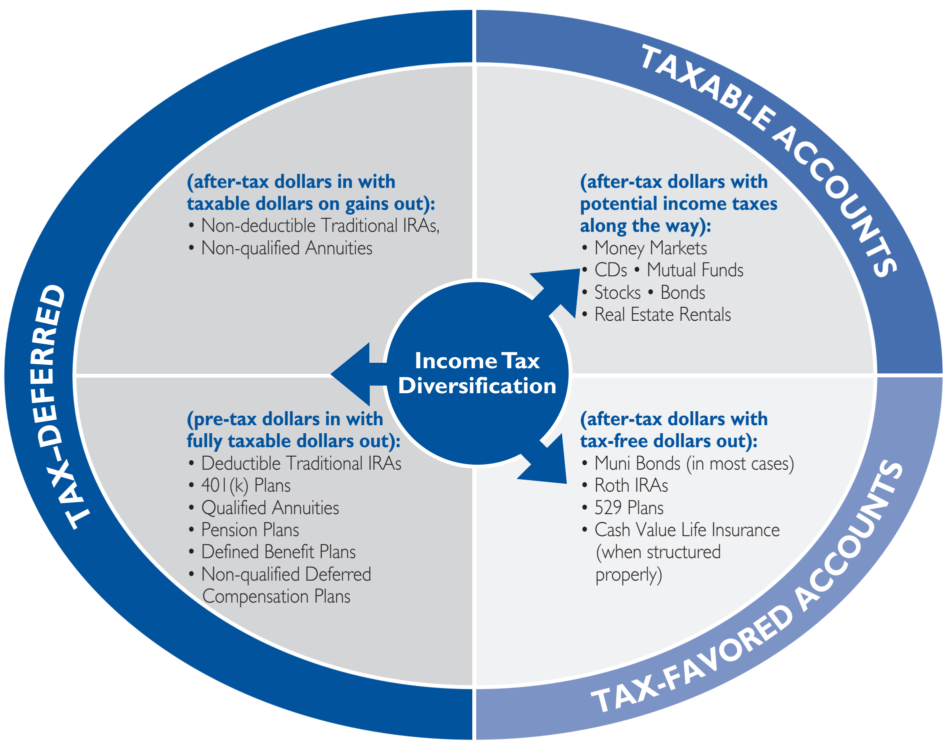
Considerations for Two of Life's Certainties

An old adage tells us that death and taxes are certainties. So how can these be addressed – especially for the long term? Putting in place valuable death benefit protection creates a core financial component when looking to your financial future and so is looking proactively at long term tax consequences. Do you want to find ways to maintain your retirement savings and pay less in income taxes? While today's economic environment continues to offer challenges, there are some important strategies to consider as you build your nest egg.

The Importance of Tax Diversification for a Strategic Retirement [1]

It is important to take income taxation into consideration as you plan for the future. If you're like many today in the midst of planning for retirement, you probably have several different types of investment accounts. These accounts tend to fall into three general categories as it pertains to how the values within them will ultimately be taxed. These categories include taxable, tax-deferred (which includes two sub-categories), or tax-favored accounts. The following chart shows how typical account types are separated into these categories.



[1] Guardian, its subsidiaries, agents or employees do not give tax or legal advice. You should consult your tax or legal advisor regarding your individual situation.

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As you approach your ultimate retirement date, where do you think income tax rates will be — especially since tax rates are at or near historical lows today? That answer is hard to determine with certainty — however, it's important to understand how these account types are taxed.

	Yearly 1099s?	Pay Taxes on Gains?	Tax Deferred?
Taxable Accounts	Yes	Yes	No
Tax-Deferred Accounts	No	Yes	Yes
Tax-Favored Accounts	No	No	Yes[2]

Here is a general summary of some of the tax considerations of various supplemental retirement alternatives:

	Contributions	Accumulation	Distributions
Certificate of Deposit	After-Tax	Taxable	Non-Taxable
Mutual Fund	After-Tax	Taxable	Non-Taxable
Muni Bond Fund[3]	After-Tax	Non-Taxable	Non-Taxable
Employee 401(k)	Pre-Tax	Tax-Deferred	Taxable
IRAs - Regular	Pre-Tax	Tax-Deferred	Taxable
Roth IRAs	After-Tax	Tax-Deferred	Non-Taxable[4]
Permanent Life Insurance	After-Tax	Tax-Deferred	Non-Taxable[5]

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[2] Life insurance has some additional advantages versus traditional tax-deferred accounts. The gain may never be taxed if the policy is held until death.

[3] This depends on the investment and may be subject to the Alternative Minimum Tax (AMT).

[4] Qualified distributions are non-taxable. Otherwise, gain is subject to ordinary income tax plus a possible 10% penalty.

[5] Withdrawals are received tax-free to the extent of premiums paid. Loans are tax-free while the policy remains in force. When a policy is surrendered, if a policy has an outstanding loan, the loan is added to the proceeds for purposes of determining the taxable gain. If the policy is a Modified Endowment Contract (MEC), the gains are taxed like a annuity, and if the insured is under age 59½ a 10% tax penalty will apply to the gain.

So what is the impact on the benefits shown in the previous chart when your money is mixed among these different categories of accounts? Well, for one thing, having dollars spread among these various account options can give you some flexibility and choice when determining how much taxation you will incur during your retirement years. Look at the following hypothetical example that shows what would happen if you take 100% of $100,000 out of a 401(k) account (after age 59½) versus taking 50% of the money out of a 401(k) and 50% out of a tax-favored asset , such as a Whole Life insurance policy.

100% 401(k) Withdrawal

	401(k)
Money Withdrawn	$100,000
Taxes Paid (28%)[6]	$28,000
Total Net Withdrawal Amount	$72,000

50% 401(k), 50% Whole Life Cash Value Withdrawal

	401(k)	Whole Life Policy Cash Values[7]	
Money Withdrawn	$50,000	$50,000	
Taxes Paid (28%)[8]	$14,000	$0	**Total Money Kept**
Net Withdrawal Amount Per Account	$36,000	$50,000	**$86,000**

The example assumes a total effective tax rate of 28% at $100,000 in income and a total effective tax rate of 28% at $50,000 of taxable income. However, remember, tax brackets may be very different in the future (and if we're at or near historic lows today which way do you think they'll go?).

▶ Based on this hypothetical example, the 50/50 option creates an additional $14,000 at retirement.[9]

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[6] Taxes are due on the 401(k) account since the money contributed to that account is on a pre-tax basis. We are assuming that the $100,000 has a client in a 28% effective tax bracket.

[7] Whole Life Insurance provides death benefit protection for the whole of life as long as the guaranteed premium is paid. With payment of the guaranteed premium you receive a guaranteed death benefit and guaranteed cash values inside the policy. *Guarantees are based on the timely payment of required premiums, and the financial strength and claims paying ability of the company, which is measured by the four major ratings services. Costs for these benefits are reflected in lower cash values in the early years of the policy. In fact, cash values may not be available in the first two policy years. In addition, dividends, which are not guaranteed, may not be paid in the first two policy years. Whole life cash accumulation should be considered for its long term values.*

[8] Taxes are due on the 401(k) account since the money contributed to that account is on a pre-tax basis. However, no taxes are due on the Whole Life cash value. We assume that the $50,000 has a client in a 28% effective tax bracket.

[9] Dollars contributed to life insurance premiums are not tax-deductible. Therefore, there may be more initial income tax benefits with other investment accounts because of tax deductibility. However, as stated in this piece, the account holder will pay ordinary income taxes on the dollars distributed from 401(k) accounts.

The Importance of Life Insurance Protection

So, you may now have a better understanding of account taxation. But to protect your family in the event of an untimely death, life insurance can be a core component of a comprehensive financial portfolio — providing both death benefit protection and valuable living benefits, such as access to policy cash values for supplemental retirement income.

One of the most common types of life insurance, and the one that has been around the longest, is Whole Life. Whole Life is a versatile financial instrument used for protecting families and businesses while creating and enhancing portfolio wealth. Whole Life insurance:

1. **Allows for lifetime insurance protection through a death benefit**
2. **Can be viewed as a comprehensive portfolio asset in a financial portfolio**
3. **Contractually maintains guarantees**[10]
4. **Offers a non-guaranteed policy dividend**[11]
5. **Can create tax advantages** – Life insurance is viewed as beneficial for society. Therefore, significant tax benefits have been bestowed on it that do not apply to most other financial instruments. These include: income tax-free death benefits, tax-deferred buildup of cash values inside the policy, and access to policy values on a tax-favored basis

Additionally, there are other advantages to life insurance versus some traditional tax-deferred retirement options for living benefit purposes:

- Funds can be withdrawn at any time without penalty
- No required minimum distribution (as with certain types of retirement plans)
- Loans can remain outstanding indefinitely
- No IRS limits on the maximum premium (other than MEC issues)

Contact your Guardian financial representative today to learn more about proactive strategies for your retirement savings and how to maintain death benefit protection for your heirs.

[10] All whole life insurance guarantees are subject to the timely payment of all required premiums by the insured and the claims paying ability of the issuing insurance company.

[11] Dividends are not guaranteed. They are declared annually by Guardian's Board of Directors.

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