Dynamic Chiropractic

YOUR PRACTICE / BUSINESS

The Chiropractic Annuity

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We all fantasize about the time of life when we can take it easy but all too often due to a lack of careful retirement planning, our fantasies never become reality.

In short, the doctor of chiropractic needs to plan for his future. There are various tools he can utilize to make the dream come true.

The DC should always consider starting with an individual retirement account (IRA), Keogh, and/or company pension plan. These are all ways to set aside money for retirement. One often overlooked vehicle, however, is the annuity which remains an extremely tax advantageous method to save money for retirement purposes. Properly structured, the annuity should allow the DC to have his savings grow tax deferred and to build that retirement fund more rapidly than through the use of other alternative investments.

What Is An Annuity?

An annuity is a method to set aside funds during the DC's working life and to have those funds grow on a tax deferred basis for future utilization. When the DC is ready to retire, it can provide regular monthly payments for the rest of his life, irrespective of how long the DC might live. One popular method to achieve this result is to invest money with an insurance company. The insurance company then insures the DC against the risk that he will outlive his retirement savings. Alternatively, if the need should arise, the DC can withdraw the funds in cash or in a series of withdrawals over a shorter specified term.

One of the major advantages is that there is no yearly investment maximum. Another is that the money will grow faster than with a taxable investment due to the fact that interest will accrue tax free until withdrawal, and money which would otherwise have been utilized to pay a tax obligation remains in an account accruing interest. There are risks. If the DC suddenly needs a substantial amount of money and withdraws funds from the annuity before he is 59-1/2, the earnings will not only be taxed, but a 10 percent penalty will be assessed by the Internal Revenue Service as well.

It should also be noted that there are no annual IRS forms. An entry on Form 1040 is not needed until the funds are being withdrawn.

Hypothetical

Let us assume that the doctor of chiropractic has reached age 70. Along the way he has made a taxable investment. Suppose he was 50 years old when the investment was made, and while in the 33 percent tax bracket he invested $25,000 into a taxable investment and, further, $25,000 more into a tax deferred annuity. Let us further assume that both investments earn a 10 percent rate of return and that withdrawals are deferred until age 70. The computations are formidable, but looking at the taxable investment with systematic withdrawals from age 70 to 90, the DC would receive $678 per month for 20 years. With respect to the annuity commencing at age 70, the DC would receive $1,040 per month for life.

Types of Annuities

If the DC places funds into an annuity and allows the funds to grow in a tax deferred manner for withdrawal at a future date, this approach is called the "deferred annuity." If the DC places funds in an annuity and begins to receive regular income immediately, this is called an "income annuity."

If the DC purchases a deferred annuity, it is possible for him to convert it into an income annuity at a future time.

Method of Payment

The DC may purchase the annuity with a single amount. This is known as a "single premium annuity." He can purchase the annuity in a series of payments. This is called a "flexible premium annuity."

Guaranteed Yield

It is possible to have the annuities grow at a preset interest rate guaranteed by the insurance carrier and, further, the insurance company will guarantee to refund the amount of principal inserted. This is called a "fixed annuity" and is also known as a "guaranteed annuity." There is also a "variable annuity" in which the specification is that the funds are invested in mutual funds. Variable annuities are also known as "self-directed annuities" because the DC would have the right to instruct the appropriate representative as to which mutual fund portfolio the money should be placed.

Watch Out for Expenses

There are expenses associated with annuities which can affect the ultimate value. In a sense, an analogy can be drawn to purchasing a time share interest which value is destroyed by outrageous monthly "association" fees. The DC should consider the charges associated with the annuities for marketing expenses, managing investments, and other miscellaneous charges such as surrender charges (could be as much as 10 percent), annual cost of administration and miscellaneous variable fees and expenses (such as a mortality and expense charge, which is a fee paid for the guarantee the company makes that the DC could never outlive his annuity income).

Annuity and Pension Plan

It is often wise to utilize an annuity with a pension plan. Imagine the situation where the DC has income flowing in from a retirement plan, social security, personal savings, and an annuity as well. It has become apparent that it is necessary to have personal savings as an additional income source.

Annuity Versus IRA

Annuities and IRAs both offer tax deferred savings. IRA contributions, however, are restricted to $2,000 annually. An annuity is not restricted. An annuity allows the investment to accumulate until age 80 or later, but with an IRA one is required to begin withdrawals at age 70-1/2 or face a penalty.

How Will the IRS Tax My Annuity Payments?

Tax treatment varies widely for annuities purchased with "before tax" dollars (such as an IRA) and most employer sponsored pension plans versus purchasing an annuity with "after tax" dollars. If it

is purchased with after tax dollars, the individual pays income tax only on the portion which represents earnings.

In any event, annuities offer an attractive alternative and an efficient way to turn capital into income primarily because of its tax advantages. Properly planned, an annuity can produce more spendable income for the DC than living off of interest alone or attempting to spread out systematic withdrawals from the investment over the lifetime of the DC.

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