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The Million-Dollar Matrix: Save a Million Dollars by the Time You Retire

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I ran some numbers recently to see what it would take to accumulate a million dollars. I call this the Million-Dollar Matrix. If you are age 35 and could earn 8 percent per year, you could build a fund of $1 million by age 65, if you deposited $667 per month. Thirty years to build $1 million, assuming you have put the money in a qualified retirement plan, since there are no taxes due every year on the interest earned.

If you are age 45, you would have to save $1,686 per month at 8 percent interest to accumulate $1 million by age 65. Twenty years to $1 million. This also assumes you are using a qualified plan to avoid taxes during the accumulation period.

OK, so you have accumulated $1 million in a retirement plan. Now what? Well, you kick back and retire with an income stream for the rest of your life. But wait: Since you did not have any taxes to pay on the interest earned during the accumulation period, now the IRS wants their "fair share" or whatever you want to call it.

To keep things very simple, let's assume your tax rate is just 30 percent. Based on that, if you took out the 8 percent earned on your $1 million every year, that would be $80,000 per year, gross. That means before taxes. Less 30 percent for taxes ($24,000) leaves you a net of $56,000 annually.

If you are age 35 when you start this plan, with a deposit of $667 per month, or $8,004 yearly, your tax savings at 30 percent would be $2,401 per year. Over the 30 years to age 65, that would total a tax savings of $72,030. Based on the fact that at age 65, your tax liability on your retirement income of $80,000 per year is $24,000 per year, you would pay back all your tax savings in just three years. If you live to just age 80, your total tax liability would be $360,000. If you are lucky enough to live to age 100, your total tax liability would be $840,000. There would probably also be an estate tax due on the balance left in the retirement plan when you die.

If you are age 45, with a monthly deposit of $1,686 or $20,232 annually, your tax savings would be $6,070 per year, or $121,400 to age 65, assuming a 30 percent tax bracket. The plan would then pay you $80,000 per year, or $56,000 net after taxes. With a $24,000 per-year tax due, it would only take a little over five years to pay back all of the tax savings.

It just doesn't seem fair to have to pay all those taxes once you retire. Are there any alternatives that can work better? Yes there are. How would you like a plan that allows you to accumulate your funds with no limits on what you can deposit into it and no requirements to make any deposits for any employees? Does any such plan exist? Actually, it does; it is an insurance product called "indexed universal life" that has within it a portfolio of indexes, such as the S&P 500, Dow Jones Industrial Average, NASDAQ 100, S&P Mid Cap 400, Dow Jones Euro Stoxx 50, and the Russell 2000. You can pick and chose the ones you want, or use a mix of all of them, and change them at any time with a phone call. You only share in the gains, not the losses. Quite a unique product.

There aren't many companies that issue indexed universal life, but it can be quite effective, especially if you overfund it with extra cash that goes in basically untouched. That is why this plan builds so much money. You can get to this cash anytime you want. There are no restrictions like they have on retirement plans. The cash builds up with no current tax liability, and you can take it out with no taxes to pay. In many states, if you get sued or file for bankruptcy, no one can get to this money.

Let's see what this will accumulate. At age 35, with the same deposit of $667 per month, at age 65 the plan could yield a retirement income of $76,200 per year to age 100. That totals more than $2.5 million. At age 45, the plan could yield $71,000 per year to age 100, for a total of more than $2.414 million. No tax savings on the annual deposits to age 65, but also no taxes due on the retirement income. Not a bad trade-off, with quite an increase in the annual retirement income when compared with a qualified retirement plan. Since these plans are life-insurance products, they also have a death benefit that would be payable to your beneficiaries at death.

Why would anyone want a regular qualified retirement plan? Maybe they like the fact that they have fees to pay every year and are required to include all employees, including the ones they wished were "ex" employees. Apparently they also enjoy dealing with the IRS and the changes that take place in plans almost every year. Does that sound like you? I didn't think so. Talk to your financial consultant for more information.

MARCH 2010