



Baystate Financial Planning

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RETIREMENT PLANNING

It's all about Choices
Are you prepared to make
the right ones?

Retirement Income

Qualified vs. Non-Qualified

Defined Contribution and/or Defined Benefit

What are the tax consequences during

CONTRIBUTION

ACCUMULATION

DISTRIBUTION

Qualified:

Tax deductible contributions. Tax-deferred Accumulation. Ordinary income distributions.

Non-Qualified:

After-tax dollars accumulated with current taxes (unless “cash value” and taxable when received, or sooner, or not at all).

QUALIFIED vs. NON-QUALIFIED



Deferral Elections:	Change during the year	Election made before beginning of calendar year (may not change during the year)
Loans:	Permitted	NOT ALLOWED
Distribution Date and Form of Payment:	Made at time of distribution	Made at time of deferral
Account Balance:	Funds allocated in the plan trust	“hypothetical” UNFUNDED
Access by Corporate Creditors:	NO	YES (general assets on the books)

CONTRIBUTIONS

Most Common Mistakes

1. Making contributions to retirement accounts without first:
 - a. providing adequate food, clothing, and shelter;
 - b. providing an emergency fund;
 - c. protecting current income; and
 - d. paying down high non-deductible interest rate debt
2. Making qualified plan contributions on April 15th for the prior year instead of gaining the benefits of 15.5 months of tax deferral by making contributions as close to January 1st of the current year
3. Not taking full advantage of employer matching contributions
4. Not making the right decision regarding which to fund first:
 - a. children's education expenses; or
 - b. your retirement -- but, should it be qualified, non-qual., or both?

CONTRIBUTIONS

Most Common Mistakes

5. Not utilizing other tax advantaged funding vehicles WHY DEFER?
6. Under-estimating how much you will need in retirement
7. Depending on other assets to fund your retirement, such as:
 - a. selling a private business; or
 - b. selling real estate, including your house
8. Over-reliance on Social Security
9. Trying to make these decisions on your own, without professional assistance
10. Procrastination -- simply not making the contributions at all

What are the choices?

	A	B	C
Contribution	pre-tax	after-tax	
Accumulation	tax-free (tax-deferred)	ordinary income (interest and ST gains)	capital gains (dividends and LT gains)
Distribution	tax-free	ordinary income 1. all distrib. 2. growth only	capital gains (dividends and LT gains)
Participation	selective	all eligible 21/1,000 hrs	

What are the choices?

Contribution	A	B	B
Accumulation	A	A	A
Distribution	B1	B2	A
Participation	B	A	A
Plan	Qualified Plans	Annuity	Roth IRA and 401(k), 529 plans, & Life Ins. cash value

Contribution/Accumulation/Distribution

	Old Paradigm:	lower tax bracket in retirement		New Paradigm:	may be in higher tax bracket
Year	Before Tax Contribution	9% Tax Deferred Accumulation	Tax Bracket	After Tax Contribution	9% Tax Deferred Accumulation
1	\$9,000.00	\$9,810.00	one-third	\$6,000.00	\$6,540.00
2	\$9,000.00	\$20,502.90		\$6,000.00	\$13,668.60
3	\$9,000.00	\$32,158.16		\$6,000.00	\$21,438.77
4	\$9,000.00	\$44,862.40		\$6,000.00	\$29,908.26
5	\$9,000.00	\$58,710.01		\$6,000.00	\$39,140.01
6	\$9,000.00	\$73,803.91		\$6,000.00	\$49,202.61
7	\$9,000.00	\$90,256.26		\$6,000.00	\$60,170.84
8	\$9,000.00	\$108,189.33		\$6,000.00	\$72,126.22
9	\$9,000.00	\$127,736.37		\$6,000.00	\$85,157.58
10	\$9,000.00	\$149,042.64		\$6,000.00	\$99,361.76
	Tax Bracket			Tax Bracket	
NET	one-third	\$99,361.76	EQUALS	one-third	\$99,361.76
NET	one-half	\$74,521.32	LESS THAN	one-half	\$99,361.76
NET	one-quarter	\$111,781.98	GREATER THAN	one-quarter	\$99,361.76

The Choice is Yours

Contribution Accumulation	Before Tax Tax-Deferred	After Tax Tax-Deferred	After Tax Tax-Deferred	After Tax Taxable
AGE	\$ 9,000 at 9%	\$ 6,000 at 9%	\$ 6,000 at 9%	\$ 6,000 at 6%
50	\$ 9,810	\$ 6,540	\$ 6,540	\$ 6,360
51	20,503	13,669	13,669	13,102
52	32,158	21,439	21,439	20,248
53	44,862	29,980	29,980	27,823
54	58,710	39,140	39,140	35,852
55	73,804	49,203	49,203	44,363
56	90,256	60,171	60,171	53,385
57	108,189	72,126	72,126	62,948
58	127,763	85,158	85,158	73,085
59	149,043	99,362	99,362	83,830
NET	\$ 99,362	\$91,490	\$99,362	\$83,830

Distribution

Taxable

Cap. Gains

Tax-free
plus ins. cost

Tax-Free

Qualified Retirement Plans -- Summary

	2002	2003	2004	2005	2006	2007	2008
Compensation	\$200,000	\$200,000	\$205,000	\$210,000	\$220,000	\$225,000	\$230,000
Defined Benefit	\$160,000	\$160,000	\$165,000	\$170,000	\$175,000	\$180,000	\$185,000
Defined Contribution	\$ 40,000	\$ 40,000	\$ 41,000	\$ 42,000	\$ 44,000	\$ 45,000	\$ 46,000
Profit Sharing	25%	25%	100%	100%	100%	100%	100%
Money Purchase*	15%	15%					
401(k) / 403(b)	\$ 11,000	\$ 12,000	\$ 13,000	\$ 14,000	\$ 15,000	\$ 15,500	\$ 15,500
Plus Age 50+	1,000	2,000	3,000	4,000	5,000	5,000	5,000
Simple	\$ 7,000	\$ 8,000	\$ 9,000	\$ 10,000	\$ 10,000	\$ 10,500	\$ 10,500
Plus Age 50+	500	1,000	1,500	2,000	2,500	2,500	2,500
IRA	\$ 3,000	\$ 3,000	\$ 3,000	\$ 4,000	\$ 4,000	\$ 4,000	\$ 5,000
Plus Age 50+	500	500	500	500	1,000	1,000	1,000

* The full 25% of compensation funding limit in 2001 or 40% in 2002 and 2003 could be funded through the Money Purchase plan. It has been customary, for greater flexibility, to fund the maximum available through the profit sharing plan and only the balance through the Money Purchase plan.

In 2008, 25% profit sharing will be sufficient to fund the full \$45,000 at \$180,000 of income.

LIFE INSURANCE

- **All of our clients want life insurance**
- **They want the life insurance to be in-force when they die**
- **They just don't want to pay for it**
 - **Split-Dollar is Alive and Well (SLOBs)**
 - **Qualified Retirement Plans**

Life Insurance in Qualified Plans

Defined Contribution

	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>
Max. Contribution	\$ 42,000	\$44,000	\$45,000	\$46,000
Max. Comp. Needed *	\$168,000	\$44,000	\$45,000	\$46,000
Life Insurance				
25% of employer contrib. for Term or Universal premium payments	\$ 10,500	\$11,000	\$11,250	\$11,500
50% for Whole Life	\$ 21,000	\$22,000	\$22,500	\$23,000

Previous years contributions and accumulations may also be used to pay life insurance premiums along with IRA funds rolled into the qualified plan

* Based on a traditional profit sharing plan with contributions as a level percentage of compensation, not integrated with Social Security

Life Insurance in Qualified Plans

Defined Contribution

Beneficiary may receive the net death benefit free of income tax consequences.

Option A: Level Death Benefit (face amount only)

- Beneficiary receives face amount less cash value
- Plan receives the cash value

Option B: Increasing Death Benefit (face amount plus cash value)

- Beneficiary receives the face amount
- Qualified Plan receives the cash value

Life Insurance in Qualified Plans

Defined Benefit

Formula: 100 x Max. Monthly Pension:

<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>
\$1,416,667*	\$1,458,333*	\$1,500,000*	\$1,541,667
\$14,167/mo.	\$14,583/mo.	\$15,000/mo.	\$15,541.67/mo.
\$170,000/yr.	\$175,000/yr.	\$180,000/yr.	\$185,000/yr.

Potential to purchase additional life insurance under Rev. Rul. 74-307

* Must be level death benefit (face amount only)

Life Insurance in Defined Benefit

Contribution For:	Owners I & II Total Contributions	Total Plan Contributions	%
A) Retirement Benefit Only No Life Insurance	\$215,400	\$293,800	73.32
B) Retirement Benefit and Life Insurance of 100 x Monthly Benefit \$1,333,300 on Owners I & II	\$226,800	\$312,400	72.60
Increase between A) and B) Income Tax Deductible @ 40%	\$11,400 \$6,840	\$18,400 \$11,040	
C) Retirement Benefit and Life Insurance \$1,900,000 on Owner I <u>\$2,400,000 on Owner II</u> \$4,300,000 (Rev.Rul.74-307)	\$230,200	\$316,400	72.76
Effective Cost of Additional \$1,633,400 of Life Insurance Increase between A) and C) Income Tax Deductible @ 40%	\$3,400 \$2,040	\$4,000 \$2,400	

Life Insurance in Qualified Plans

Defined Benefit

Instead of Plan Contributions, if Owners received compensation:

\$312,400	Taxable Income
<u>(124,960)</u>	TAX (40%)
\$187,440	NET

Instead, with Plan Contribution of \$312,400:

\$226,800	Contribution for Owners
\$ 39,360	<u>NO COST -- GAIN!</u>

Life Insurance in Qualified Plans

Tax Deductible Buy/Sell Agreements

Profit Sharing:

The participant can insure anyone with whom they have an insurable interest.

- the participant
- spouse
- survivorship
- business partner

Defined Benefit:

Insurance must be on the life of the participant. Use for “indirect” funding (employee benefits) to reduce the “direct” buy/sell funding.

Ledger using Enterprise Executive Advantage

Variable Universal Life Insurance Illustration

Prepared for the Company

Martha Washington, Female Preferred Non Smoker, Age 47

Initial Face Amount: \$2,029,341

Adjustable Term: \$0

Initial Annual Premium: \$103,810.00

Death Benefit: Face + Cash Value

Initial Underwriting: Fully Underwritten

Corporation Tax Bracket: 40%

Loan Interest Rate: 4.75% in arrears

Hypothetical Rate: 7.29%(Net) 8.00%(Gross)

Cost of Money: 0% Discount Rate: 0%

Definition of Life Ins.: Guideline

Standard Illustration Using Current Charges assuming Arithmetic Average

Policy Year	Age Beg of Year	Total Policy Premium	Partial Surrender & Withdrawals from Ins. Contract	Annual Loan	Loan Interest	After-Tax Insurance Outlay	Net Cash Surrender Value	Cash Value	Net Death Benefit After Loans
1	47	103,810	0	0	0	103,810	105,635	97,531	2,126,872
2	48	103,810	0	0	0	103,810	209,712	201,407	2,230,748
3	49	103,810	0	0	0	103,810	311,973	311,973	2,341,314
4	50	103,810	0	0	0	103,810	421,641	421,641	2,450,982
5	51	103,810	0	0	0	103,810	537,996	537,996	2,567,337
		519,050	0	0	0	519,050			
6	52	103,810	0	0	0	103,810	662,243	662,243	2,691,584
7	53	103,810	0	0	0	103,810	795,530	795,530	2,824,871
8	54	103,810	0	0	0	103,810	944,512	944,512	2,973,853
9	55	103,810	0	0	0	103,810	1,105,024	1,105,024	3,134,365
10	56	103,810	0	0	0	103,810	1,278,383	1,278,383	3,307,724
		1,038,100	0	0	0	1,038,100			
11	57	0	146,953	0	0	-146,953	1,201,026	1,201,026	3,160,771
12	58	0	146,953	0	0	-146,953	1,118,185	1,118,185	3,013,818
13	59	0	146,953	0	0	-146,953	1,029,658	1,029,658	2,866,865
14	60	0	146,953	0	0	-146,953	935,042	935,042	2,719,912
15	61	0	146,953	0	0	-146,953	833,870	833,870	2,572,959
		1,038,100	734,765	0	0	303,335			
16	62	0	146,953	0	0	-146,953	727,398	727,398	2,426,006
17	63	0	146,953	0	0	-146,953	613,361	613,361	2,279,053
18	64	0	9,429	137,524	0	-146,953	490,229	634,286	2,125,567
19	65	0	0	153,485	6,532	-146,953	357,110	661,942	1,964,791
20	66	0	0	160,776	13,823	-146,953	213,104	686,349	1,796,378
		1,038,100	1,038,100	451,785	20,355	-431,430			
21	67	0	0	21,460	21,460	0	219,807	715,531	1,773,899
22	68	0	0	22,479	22,479	0	226,710	745,961	1,750,352
23	69	0	0	23,547	23,547	0	233,740	777,676	1,725,667
24	70	0	0	24,665	24,665	0	240,809	810,583	1,699,850
25	71	0	0	25,837	25,837	0	247,962	844,800	1,672,766
		1,038,100	1,038,100	569,774	158,344	-431,430			
26	72	0	0	27,064	27,064	0	254,812	880,000	1,644,436
27	73	0	0	28,350	28,350	0	261,186	916,070	1,614,739
28	74	0	0	29,696	29,696	0	267,011	953,002	1,583,632
29	75	0	0	31,107	31,107	0	272,455	991,031	1,551,048
30	76	0	0	32,585	32,585	0	277,704	1,030,412	1,516,916
		1,038,100	1,038,100	718,576	287,146	-431,430			
31	77	0	0	34,132	34,132	0	282,642	1,071,103	1,481,162
32	78	0	0	35,754	35,754	0	286,971	1,112,884	1,443,710
33	79	0	0	37,452	37,452	0	290,385	1,156,530	1,404,479
34	80	0	0	39,231	39,231	0	292,738	1,198,977	1,363,365
35	81	0	0	41,094	41,094	0	293,767	1,243,052	1,320,338
		1,038,100	1,038,100	906,239	474,809	-431,430			

The hypothetical rate of return is illustrative only to show how the performance of the underlying investment accounts would affect the policy cash value and death benefit and should not be deemed a representation of past or future investment rates of return.

The values are based on a hypothetical rate of return and an average of the advisory fees and operating expenses of each of the investment accounts underlying New England Life Insurance Company's Variable Life Insurance policies. The average reflects fee waiver and expense reimbursement arrangements that may be voluntary and of limited duration. Without these benefits, results would be less favorable. The average for expenses used in the illustration is 0.66%. This illustration does not show policy values allocated to the Fixed Account.

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Ledger using Enterprise Executive Advantage

Variable Universal Life Insurance Illustration

Prepared for the Company
 Dolly Madison, Female Preferred Non Smoker, Age 37
 Initial Face Amount: \$2,747,768
 Adjustable Term: \$0
 Initial Annual Premium: \$101,536.00
 Death Benefit: Face + Cash Value
 Initial Underwriting: Fully Underwritten

Corporation Tax Bracket: 40%
 Loan Interest Rate: 4.75% in arrears
 Hypothetical Rate: 7.29%(Net) 8.00%(Gross)
 Cost of Money: 0% Discount Rate: 0%
 Definition of Life Ins.: Guideline

Standard Illustration Using Current Charges assuming Arithmetic Average

Policy Year	Age Beg of Year	Total Policy Premium	Partial Surrender & Withdrawals from Ins. Contract	Annual Loan	Loan Interest	After-Tax Insurance Outlay	Net Cash Surrender Value	Cash Value	Net Death Benefit After Loans
1	37	101,536	0	0	0	101,536	103,544	95,421	2,643,169
2	38	101,536	0	0	0	101,536	205,449	197,326	2,945,094
3	39	101,536	0	0	0	101,536	305,864	305,864	3,053,632
4	40	101,536	0	0	0	101,536	416,087	416,087	3,163,855
5	41	101,536	0	0	0	101,536	532,838	532,838	3,280,606
		507,680	0	0	0	507,680			
6	42	101,536	0	0	0	101,536	656,512	656,512	3,404,280
7	43	101,536	0	0	0	101,536	787,586	787,586	3,535,354
8	44	101,536	0	0	0	101,536	931,919	931,919	3,679,687
9	45	101,536	0	0	0	101,536	1,088,323	1,088,323	3,836,091
10	46	101,536	0	0	0	101,536	1,259,821	1,259,821	4,007,589
		1,015,360	0	0	0	1,015,360			
11	47	0	151,515	0	0	-151,515	1,178,219	1,178,219	3,856,074
12	48	0	151,515	0	0	-151,515	1,091,070	1,091,070	3,704,559
13	49	0	151,515	0	0	-151,515	998,062	998,062	3,553,044
14	50	0	151,515	0	0	-151,515	898,795	898,795	3,401,529
15	51	0	151,515	0	0	-151,515	792,817	792,817	3,250,014
		1,015,360	757,575	0	0	257,785			
16	52	0	151,515	0	0	-151,515	681,440	681,440	3,098,499
17	53	0	106,270	45,245	0	-151,515	561,986	609,380	2,944,835
18	54	0	0	153,664	2,149	-151,515	433,029	641,367	2,783,871
19	55	0	0	160,963	9,448	-151,515	293,791	670,757	2,615,262
20	56	0	0	168,609	17,094	-151,515	143,497	697,081	2,438,645
		1,015,360	1,015,360	528,481	28,691	-499,790			
21	57	0	0	25,103	25,103	0	148,618	728,498	2,412,349
22	58	0	0	26,295	26,295	0	153,769	761,193	2,384,805
23	59	0	0	27,544	27,544	0	158,917	795,194	2,355,952
24	60	0	0	28,853	28,853	0	164,111	830,611	2,325,729
25	61	0	0	30,223	30,223	0	169,380	867,539	2,294,071
		1,015,360	1,015,360	666,499	166,709	-499,790			
26	62	0	0	31,659	31,659	0	174,744	906,065	2,260,908
27	63	0	0	33,163	33,163	0	180,053	946,112	2,226,170
28	64	0	0	34,738	34,738	0	185,284	987,731	2,189,782
29	65	0	0	36,388	36,388	0	190,324	1,030,886	2,151,666
30	66	0	0	38,116	38,116	0	195,028	1,075,517	2,111,740
		1,015,360	1,015,360	840,562	340,772	-499,790			
31	67	0	0	39,927	39,927	0	199,356	1,121,669	2,069,916
32	68	0	0	41,823	41,823	0	203,395	1,169,518	2,025,107
33	69	0	0	43,810	43,810	0	207,087	1,219,100	1,980,216
34	70	0	0	45,891	45,891	0	210,376	1,270,459	1,932,145
35	71	0	0	48,071	48,071	0	213,162	1,323,600	1,881,791
		1,015,360	1,015,360	1,060,084	560,294	-499,790			

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ACCUMULATIONS

Most Common Mistakes

1. Improperly rolling over funds from a prior employer's plan
 - a. IRAs give you a wider array of choices, but funds may be accessible by creditors (protected federal, and some states)
 - b. new employer's plan may limit choices, but provides creditor protection (federal and state)
 - c. Should you pay the tax now at lower income taxes, then what?
2. Not developing an "investor policy statement" covering level of risk and time horizon
3. Not developing a proper asset allocation
 - a. certain asset classes are better inside a tax-deferred plan
 - b. others are better being held in your taxable account

Investment Policy Statement

Abigail

4

1

2

5

3

1 = highest priority

Growth

Safety

Liquidity

Income

Tax Benefits

John

1

3

4

5

2

A:
3

J:
7

Conservative

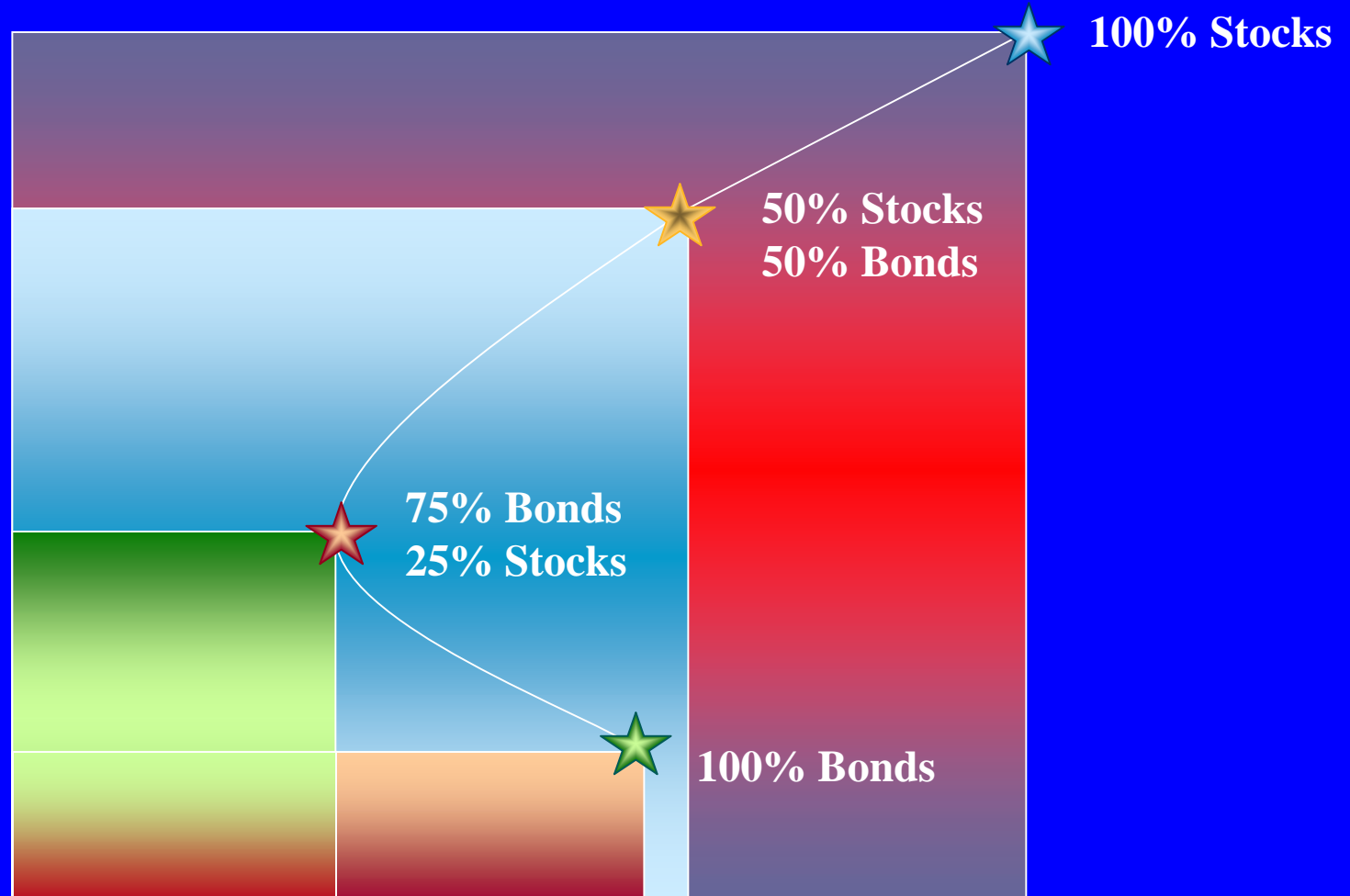
Moderate

Aggressive

Time Horizon: for retirement from age 65 to 95 (we hope)
currently age 45/43

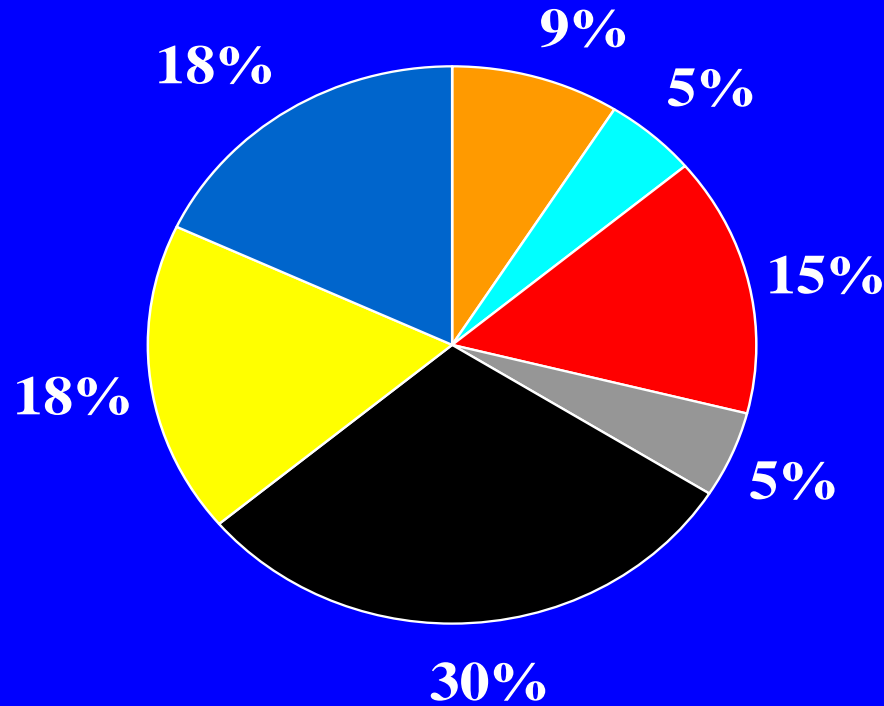
Efficient Frontier

Return



Risk

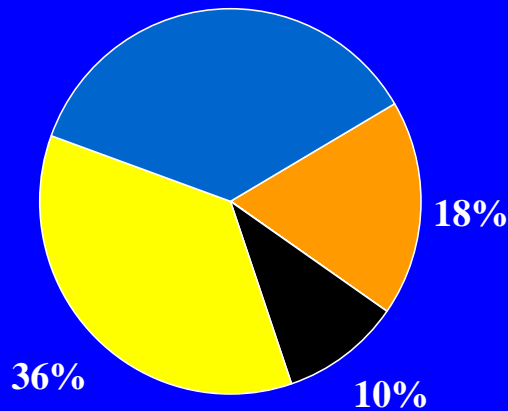
Portfolio Allocation - Capital Growth



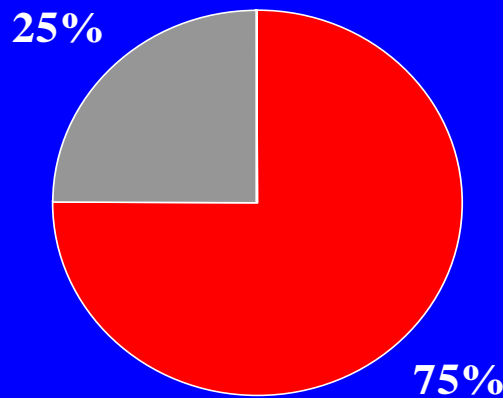
\$1,000,000



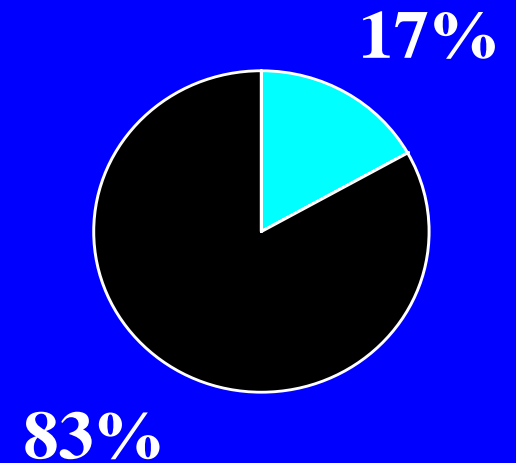
John's Qualified
\$500,000



Abigail's Qualified
\$200,000



Non-Qualified
\$300,000



ACCUMULATIONS

Most Common Mistakes

4. Not developing a successful investment strategy for retirement using qualified employer sponsored plans, including Solo(k) for “cottage industry” income
5. Over-loading your retirement account with your employer’s stock
6. Thinking that you need to shift to all cash as you approach retirement, instead of planning for the rest of your life
7. Thinking that the biggest risk is loss of principal, instead of loss of purchasing power
8. Taking on too much risk, trying to recover from recent losses
9. Trying to make these decisions on your own, without professional assistance
10. Procrastination -- simply keeping it all in the money market

DISTRIBUTIONS

Most Common Mistakes

1. Not reviewing the pros and cons of selecting a joint and survivor income stream vs. single life income plus life insurance
2. Not making a proper beneficiary designation
 - a. still names former spouse or parents/siblings
 - b. if married and name other than spouse, need written consent
 - c. doesn't provide for "stretch" IRA income tax deferral
3. Planning for "stretch" IRA when, in reality, the beneficiaries plan to take withdrawals for their lifestyle
4. Not considering estate taxes and costs of long-term care
5. Not paying back a plan loan before rollover -- taxable distribution

DISTRIBUTIONS

Most Common Mistakes

6. Taking loans from plan assets without considering other choices
7. Taking distributions before 59.5 and incurring taxes and penalties vs. accessing non-qualified deferred comp. proceeds first
8. Not taking minimum required distributions at age 70.5
9. Trying to make these decisions on your own, without professional assistance
10. Procrastination -- simply taking distributions without a plan

The contents of this presentation are intended for education purposes only.

The presentation provides a brief summary based on our understanding and interpretation of current law.

All tax references are to federal tax law only, unless otherwise stated.

This presentation includes changes made by the 2001 Tax Act.

All these changes are to expire at the end of 2010.

Pursuant to IRS Circular 230:

The information contained in this material is not intended to, and cannot be used to, avoid IRS penalties.

This material supports the marketing and promotion of life insurance.

Seek advice based on your particular circumstances from independent tax, legal, accounting, insurance, investment, and financial advisors.

Individuals, including business owners, should not apply any of these concepts without coordinating with attorneys, accountants, life insurance agents, investment advisors, financial planners, etc.

Consult with your professional tax advisor about your personal situation before making any decisions.

This is not intended to provide tax or legal advice.

Advisors should not apply any of these concepts to their clients without:

- (1) establishing a mutually agreed upon scope of their engagement;
- (2) gathering necessary and sufficient objective and subjective data given the client's goals, needs, and priorities; and
- (3) evaluating that data and determining alternative strategies consistent with the mutually agreed upon scope of the engagement and the data collected.

**Herbert K. Daroff, J.D., CFP® is a Registered Investment Advisor in Massachusetts
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