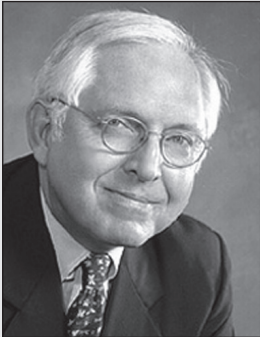


Rise of Roth IRA in the Workplace

Michael Shumway



Michael D. Shumway, CFP, CLU, is a 14-year member of MDRT with 14 Top of the Table qualifications. He has served on a variety of MDRT committees, including the Program General Arrangements Committee and Program Development Committee, and he currently is a member of the Top of the Table Web Site Content and Communications Task Force. The owner of Shumway Financial Planning, he is a partner in Magellan Financial Group, LLC. Shumway is an active member and officer of the Corpus Christi Association of Insurance and Financial Advisors.

*Shumway Financial Planning
5525 S. Staples, Suite B2
Corpus Christi, TX 78411
Phone: 361.906.2300
E-mail: michael@shumwayfinancial.com*

I/R Code: 3490.00
Cassette: A0540
CD: C0540

I have discovered a new marketing plan based entirely on my MDRT experience. It is essential that you attend every annual meeting to learn about what is new in retirement planning and tax laws. At the 2002 Annual MDRT Meeting held in Nashville, Tennessee, Ed Slott and John Bledsoe shared their knowledge and experience about Roth IRA with us. It became evident to me that we needed to think differently about pre and post retirement planning.

In 1962, at my old firm, we created the 403(b) market in Texas public schools. In the 80's we developed the one check billing system for 403(b) Plans in public schools, which helped to control the market. The state of Texas passed a law in 1986 that allowed anyone to sell 403(b) Plans in the schools. We came up with Section 125 Plans on the one check billing system. The outside agents were not very pleased because we enrolled 403(b) and Section 125 Plans simultaneously.

Another law was passed that stated that you could not be a TPA for Section 125 Plans and market 403(b) Plans at the same time. Undaunted by this new law, we then began to market 457 Deferred Compensation Plans instead of 403(b) Plans. My knowledge came from our firm opting Galveston County and Texas City out of Social Security into 457 deferred compensation. Privation works! It is my hope that Congress makes that option available once again in the near future.

In 1990, Congress passed a law requiring counties, cities, and schools to pay retirement for part time employees by method of Social Security, 403(b), or 457. Our firm came up with a 3121 Plan using 457. That led to meeting at 20 regional educational service centers in Texas for school business managers to solve the problem. It saved the school 6.2 % that they would have had to pay into Social Security for each employee. When I held the meetings at the educational service centers, we picked up new business for 3121 Plans as well as for Section 125 and 457 Plans.

The new marketing plan for my firm is to ask for Roth IRA plans on payroll. Why Roth? Simply put, it is new and different. If I go to a school and ask, "Who has a Roth

Rise of Roth IRA in the Workplace *(continued)*

payroll slot,” the Superintendent or Business Manager will say, “What are you talking about?” That is when I tell them that we have been doing retirement plans for years with pre-taxed figures, but had never thought about what the taxes coming out of the 403(b), 457, 401(k), and IRA Plans would amount to. That is when I hand out our marketing piece, and ask, “If you knew the IRS could get the majority of your retirement plan, when would you want to know about it?”

The Rise of the Roth Ira in the Workplace: A Tax Diversification Tool for the 21st Century - Agenda

- Preparing for Retirement
- Traditional Retirement Vehicles Available to Educators
- Why the Roth IRA? -Understanding the Tax Problem & Tax Diversification

Are Americans Ready for Retirement?

- 61% of all workers between the ages of 24 and 64 do not have a retirement account.
- The average retirement account is \$34,700. The median account value is only \$14,000.
- Will we have enough money to fund our retirement?

What About Educators?

- Educators retiring a standard Retirement Annuity from TRS will typically receive less than 60% of their ending salary
- The average person needs 80% or more of their pre-retirement income in order to have a comfortable retirement. How will they bridge the gap?
- The difference must come from an individual's personal savings efforts!

Traditional Retirement Vehicles Available to Educators

- Available through School District Payroll
 - TRS-Mandatory Contribution
 - 403(b)-Following TRS Guidelines
 - 457-Employer Sponsored Plan

- Available outside the Workplace
 - Traditional IRA's
 - Roth IRA's
 - Bank & Brokerage Accounts

Why the Roth IRA?

- The need for the Roth IRA on Payroll
 - Effective Savings Habits – Pay yourself first, using Payroll Deduction
 - Ease of Implementation and Maintenance
- The Need for the Roth IRA
 - The Taxation of Retirement Plans
 - The Need for Tax Diversification

The Tax Problem

- If you knew the IRS could get the majority of your retirement plan, when would you want to know about it?

Taxation in Retirement Plans

- Federal & State Income Taxes: 10-45%
- Too Soon Penalty: 10%
- Too late Tax: 50%
- Current Federal Estate Tax: 37-55%
- Current State Estate Tax: 0-6%

This could size up to a 75% shrinkage! What have you done to reduce this shrinkage?

Typical Retirement Income Strategy

- During working years, maximize contribution to retirement plans:
 - Distributions are fully taxable income.
 - At death, they may face income and estate taxation.
 - At retirement convert equities to fixed investments:
 - Bonds and other fixed investments have consistently under-performed.
 - A fixed income portfolio will decline in purchasing power by 44% in 20 years.
- Thank you, Senator Roth

Rise of Roth IRA in the Workplace *(continued)*

A Brief Overview of the ROTH IRA

- On January 1, 1998, Congress launched the last great golden opportunity of the century for Americans: The Roth IRA.
- Named after the Delaware Senator William Roth who proposed to expand IRAs as part of the Tax Reform Act of 1997.
- During planning in Congress known as the “American Dream” IRA.

Think of Two Tax Buckets 403(b)/457/ Traditional IRA

- Tax deductible on deposits
- Tax deferred on growth
- Withdrawal taxable on entire account

Roth IRA

- Taxable in
- Tax Deferred growth
- Tax free Withdrawals

Taxation of Retirement Plans

- Would you rather pay taxes on The Seed (new strategy) or The Whole Crop (typical strategy)?

Smith & Jones Family Example

Assumptions & Disclosures

Our example involves two couples that begin at 25 years of age to deposit into IRAs and continue until they are 65. Assumptions are based on the fact that the individuals’ objectives are to live on their retirement dollars instead of passing it on to their heirs. The data assumes the reinvestment of income. Assumed growth is 8% annually and does not account for any management fees and/or for transaction costs. The assumed annual withdrawal is \$60,000 after taxes. Income tax (federal, state, and local) is calculated using 27% on Roth IRA deposits and 35% on IRA withdrawals. Roth IRA withdrawals are tax free due to being taxed prior to deposits. Annual withdrawals occur after annual growth is calculated. This example assumes there are no limitations, restrictions, or surrender charges

on withdrawals. This hypothetical example is for illustrative purposes only and is not indicative of any investment. Past performance is no guarantee of future results. Investments made into variable products may be worth more or less than contributions at withdrawal.

Accumulation Phase

Roth IRA

- Smith Family: Pre-Retirement
 - Contributions are made: after tax
 - Annual Contributions: \$3,000
 - Pre-Tax Savings: None
 - Deposits to Age 65: \$120,000
 - Gross Value at Age 65: \$839,343.

Traditional IRA/403(b)/457 Plan

- Jones Family: Pre-Retirement
 - Contributions are made: before tax
 - Annual Contributions: \$4,110
 - Pre-Tax Savings: \$1,110
 - Deposits to Age 65: \$164,000
 - Gross Value at Age 65: \$1,149,900.

Distribution Phase

Roth IRA

- Smith Family: During Retirement
 - Income Stream (Age 66-100): \$60k/yr after tax
 - Total net income (Age 66-100): \$2,100,000
 - Age that money runs out: Doesn’t
 - Legacy at Death: \$1,243,846
 - Total Income to age 100: \$3,463,846

Traditional IRA/403(b)/457 Plan

- Jones Family: During Retirement
 - Income Stream (Age 66-100): \$60k/yr after tax
 - Total Net Income (Age 66-100): \$1,130,795
 - Age that money runs out: Age 84
 - Legacy at Death: None
 - Total Income at age 100: \$1,295,195
- Net difference is \$2,168,651!

Rise of Roth IRA in the Workplace *(continued)*

The Future of Taxes

- Is a financial Storm coming?

References and Recommended Reads

- **The Coming Generational Storm** by Laurence J. Kotlikoff and Scott Burns
- **The Retirement Savings Time Bomb...And How to Defuse It** by Ed Slott
- **Running on Empty** by Peter G. Peterson
- **Rich Dad's Prophecy** by Robert T. Kiyosaki with Sharon L. Lechter

In Summary

- The Need For Tax Diversification will continue to grow
 - Don't put all your eggs in one "Tax" Basket
- Potential future legislation will likely make Roth IRA's even more popular
 - Roth 403(b)? Roth 401(k)? LSA'?
- Ease of Implementation and Administration make it an easy choice for employers to give employees more options to save for retirement.

Selecting a Product for your Roth IRA: Understanding the product that will be offered to District Employees through Payroll Deduction

The Bull Market

- We all like the Bull Market!

The Bear Market

- We all hate the Bear Market!

The Chicken Market?

- But over the last 5 years, a new symbol has evolved; the market has made us chickens!

Las Vegas

- When we go to Las Vegas for a week, we like winning but don't like losing. If you lose, you get to leave with the money you came with. If you win, you get to keep most, but not all of it.

Tic-Tac-Toe

- Introduce the basic Equity Indexed Annuity Concept using tic-tac-toe...trying to find a product that provides some safety and opportunity for greater returns.

But first, what is annuity?

- A tax-deferred annuity is a long-term investment that may be an appropriate way to supplement your other retirement investing
- An annuity is a contract between you and an insurance company. You pay income tax on the money before you invest it in a tax-deferred annuity, but you don't pay income tax on the earnings until you take them out.
- Tax-deferred annuities are either fixed or variable annuities.

What is an Equity-Indexed Annuity?

- An innovative fixed annuity that offers upside potential with downside protection
- Attractive to investors seeking a product that provides some guarantees that you won't lose money, but can participate in a large percentage of gains when the market is doing well.

More on the Equity-Indexed Annuity...

- A type of Fixed Annuity that differs from others because of the way it credits interest to your annuity's value.
- It earns interest and/or provides benefits that are linked to an external equity reference or an equity index.
- One of the most commonly used indices is the S&P 500 Composite Stock Price Index.
- When you buy an equity-indexed annuity, you own an insurance contract.
- You are not buying shares of any stock or index.

Rise of Roth IRA in the Workplace *(continued)*

Key Features of an Equity-Indexed Annuity (EIA)

- They guarantee principal
- They guarantee minimum interest rate
- They offer some participation in growth, if any, of a stock market index.
- The value of the annuity is adjusted at predetermined times to reflect any index changes.

How well does the EIA Measure up against other options? Let's take a look.

- Method of Growth
 - Fixed Rate: Set rate of return
 - Variable: Investor selects one or more "mutual funds:
 - EIA: Tied to increases in the S&P 500
- Guaranteed Rate
 - Fixed Rate: Yes
 - Variable: No
 - EIA: No
- Minimum Guarantee
 - Fixed Rate: Yes
 - Variable: No
 - EIA: Yes
- Potential for Loss
 - Fixed Rate: No
 - Variable: Yes
 - EIA: No
- Potential for Gain
 - Fixed Rate: Modest
 - Variable: Great
 - EIA: Modest to Very Good
- Access to Money
 - Fixed Rate: Very Good
 - Variable: Very Good
 - EIA: Poor to Very Good

The EIA versus Mutual Funds

- Method of Growth
 - Stock Funds: Based on the stocks in the portfolio
 - Bond Funds: Based on the bonds in the portfolio
 - EIA: Tied to increases in the S&P 500

- Guaranteed Rate
 - Stock Funds: No
 - Bond Funds: No
 - EIA: No
- Minimum Guarantee
 - Stock Funds: No
 - Bond Funds: No
 - EIA: Yes
- Potential for Loss
 - Stock Funds: Yes
 - Bond Funds: Yes
 - EIA: No
- Potential for Gain
 - Stock Funds: Great
 - Bond Funds: Usually Modest
 - EIA: Modest to Very Good
- Access to Money
 - Stock Funds: Excellent
 - Bond Funds: Excellent
 - EIA: Poor to Very Good

In Summary

For individuals who are looking for a product that provides some guarantees on their principal, but who don't want to miss out on the market returns, an Equity Indexed Annuity might be an ideal choice.

Product Provider Selection

If you are going to market Roth IRAs, you need a company that will accept monthly deposits of \$25 or \$50. The company needs to do the billing for the plan. Mutual Funds should be offered in addition to index annuity. The chosen company should offer enrollment help. Agent commission can be advanced on monthly business. If enrollment help is needed you will have to split commission with the enrollment team.

Group Targeting

My main market is public schools in Texas with over 1000 school districts. The amount of public schools varies in each state. Nonetheless, they are a good starting

Rise of Roth IRA in the Workplace

point. Private schools, Churches, Colleges, Universities, Jr. Colleges, and non-profit organizations are also good to call on for the Roth IRA. My general approach is to ask each entity about their retirement plans. This not only gives me insight into what kind of financial goals they may have in mind, but it also allows me to determine if their current provider is meeting their financial planning needs and directing them down the smartest path possible. You can pick up new accounts on existing 403(b), 457, and 401(k) plans if a group is not satisfied with their current provider.

Identifying and Educating the Decision making Individual

The most difficult part is getting to the right decision maker. At a school district, start with the superintendent, director of human resources, or the business manager. At a business, start with the owner, business manager, or director of human resources.

Establishing a Payroll Slot

One of the most important rules for establishing Roth IRAs is getting on the good side of the payroll department. The payroll department must inform you about important dates, such as, when monthly cut-off dates for enrollment are scheduled. It is my duty to ensure that the payroll department knows the amount of deductions that are taken after tax. A billing sheet is given to the payroll department listing the company address where payments are remitted.

Scheduling Educational Employee Meetings

Once the case is approved and payroll is setup, next is the enrollment. Enrollment meetings require the employer or school district to set up a meeting for the employees at each establishment or school. The department head or school principal needs to make certain that all employees attend the meeting. To help expedite the process, my staff calls to confirm the scheduled date, time, and location of the meeting. They remain in contact the entire time to make certain that all necessary preparations are carried out accurately and efficiently.

Scheduling Educational Workshops

After enrollment for Roth IRAs we try to set up three-part educational workshops for employees and their spouses. The workshops give us an opportunity to attain additional assets from employees. We provide a detailed explanation for the Jumbo Roth concept. Anyone who wants to set aside more than \$500 a month is shown the Bill Nelson Life School concept. At the 2002 MDRT meeting held in Las Vegas, I had the opportunity to moderate Bill Nelson's session. I learned how to use variable life insurance as an after-tax savings plan. The average plan that I set up is \$1000 a month, which is deducted from their payroll.

Group Administration

The employer needs to know who to call with questions or problems. My staff assists me in handling all applications and service problems.

Generating Rollover and Plan Completion Business

When meeting with employees you will need to ask for copies of their existing 403(b), 457, 401(k), IRA, and non-qualified plans. You may be able to pick up these plans if they are not satisfied with their current agent. After reviewing the plans, you may be able to reposition assets into new plans that you have. This is a perfect opportunity to ask the employee if they would to complete their retirement savings goal by adding life insurance on top of their Roth IRA. I offer Long-Term Care and Critical Illness and make arrangements with the employer to set up these plans on payroll deduction.

Generating Additional Group Sales

It has been my experience when setting up a Roth IRA, that the simplest way to find out if an employer is satisfied with their current plan is to inquire. Ask a lot of questions of the employer! It's a great opportunity to find out what plan they have. The employer may be unhappy with their current plans or want a comparison of existing Section 125, 401(k), 403(b), 457, and health insurance plans. If you don't sell plans, you can either broker with someone who does, or simply refer them to someone who does. The Roth IRA can open many favorable selling opportunities and I hope it helps get you to the Top of the Table!