Money Matters

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Skloff Financial Group Question of the Month

By Aaron Skloff, AIF, CFA, MBA

Q: My spouse died as an active duty member of the U.S. military. Can I deposit some or all of the insurance proceeds I received into a tax free account?

A: The Problem - Creating Your Own Retirement Nest Egg When the Spouse of an Active Duty Military Member Spouse Dies
Making sound financial decision in the face of devastation can be very difficult. The loss of a spouse, can be emotionally and financially devastating. Your plans for a retirement nest egg can be destroyed.

The Solution - The Heroes Earnings Assistance and Relief Tax (HEART) Act of 2008
Active duty military, ready reservists and related personnel can purchase low cost group life insurance from Servicemember's Group Life Insurance (SGLI) in increments of $50,000 up to a maximum of $400,000. In addition, the federal government pays a lump sum $100,000 payment called a death gratuity if a service member dies in the line of duty. This is a free benefit that does not require the service member to pay any premiums. Both the life insurance and death gratuity proceeds pass to the beneficiary on a tax free basis.

Under most circumstances annual contributions to Roth IRAs are limited to the lesser of earned income or $5,500 for those under the age of 50, or $6,500 for those age 50 and over. The HEART Act (section 109) allows the surviving spouse to rollover all or a portion of the life insurance proceeds, the death gratuity or both into a Roth IRA or Coverdell educations savings account (section 530(d)(9)). There is a one year window to complete the transaction. **This can translate into $500,000 lump sum Roth IRA contribution and the creation of your own retirement nest egg.**

Retirement Nest Egg Versus Golden Retirement Nest Egg - The Power of a $500,000 Lump Sum Roth IRA Contribution
Roth IRAs are considered the holy grail of retirement savings vehicles since they provide for tax free growth and tax free withdrawals if the account has been open for at least five years and the owner is at least age 59 ½ or over. You can withdraw contributions, your principal, at any age on a tax free and penalty free basis.

In the following example, we look at how the $500,000 proceeds described above could growth over 25 years at a 7% rate of return in a taxable investment account (**Retirement Nest Egg**) versus a Roth IRA (**Golden Retirement Nest Egg**). In the investment account, the earnings are subject to a 25% tax rate while in the Roth IRA the earnings grow tax free. As seen in the table below, after 25 years the invest account has grown to $1.79 million while the Roth IRA has grown to $2.71 million. Through the power of compound interest and tax free grown the Roth IRA is worth almost $1 million more than the investment account – creating a Golden Retirement Nest Egg.

$500,000 Roth IRA Contribution HEART Act: Value After 25 Years, Earning 7% Per Year, 25% Tax Rate	
Investment Account Retirement Nest Egg	**Roth IRA Golden Retirement Nest Egg**
$1,796,894 Value After 25 Years	**$2,713,716 Value After 25 years**
www.skloff.com	

Additional Advantages of a Roth IRA
In addition to tax free growth and withdrawals, Roth IRAs are exempt from required minimum distributions (RMDs) for the original owner and their surviving spouse. Non-spousal, inherited Roth IRAs provide tax free growth and withdrawals, but are subject to RMDs.

Action Steps – Contribute $500,000 to a Roth IRA and Create a Golden Retirement Nest Egg
Take advantage of the HEART Act by contributing $500,000 to a Roth IRA, creating a Golden Retirement Nest Egg. Work close with your Register Investment Adviser (RIA) to be sure the transaction is completed correctly and the Roth RIA is invested appropriately.

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