



WEALTH MANAGEMENT Quarterly

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KISSING YOUR PARTNER GOOD-BYE

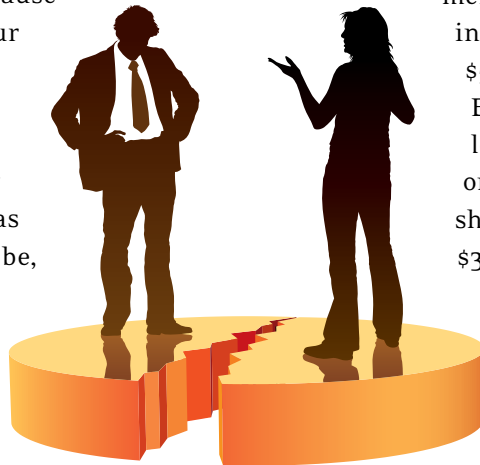
By William T. Knox IV CFA, CFP®, JD, Wealth Manager and Eric Furey, Analyst

If you participate in a tax-qualified retirement plan or make pre-tax IRA contributions, you have an investment partnership with the government. It's a great partnership, because it in effect allows your share of the partnership to grow tax-free. (Yes, we do mean tax-free, not tax-deferred - stay tuned.) But as good as this partnership may be, 2010 may be the right time to kiss your government partner goodbye. Let's begin with basic retirement savings math. Consider two individuals, Bob and Mary, both subject to federal and state ordinary income taxes at a 33% marginal rate and capital gains taxes at 20%. Bob collects a \$15,000 bonus, pays \$5,000 in taxes, and invests the \$10,000 balance in a growth stock (he hopes) paying no dividends. It's a good long-term pick, and after many years when it's worth \$30,000 Bob sells it, pays \$4,000 of capital gains tax, and nets \$26,000. Mary defers her \$15,000 bonus into her 401(k) account and invests it in the same stock. After many years, when her \$15,000 has grown to \$45,000, she sells it, withdraws the \$45,000 from the plan, pays \$15,000 of income tax, and nets \$30,000.

Why does Mary wind up with \$4,000 more than Bob? Simply because she agreed

to let the government be her partner in her 401(k) account. When the \$15,000 went into her account, it was in effect her own \$10,000 plus the government's \$5,000. By not giving the government their \$5,000 immediately like Bob did, but instead allowing them to piggyback on her stock investment, she grew her \$10,000 to \$30,000 while growing the government's \$5,000 to \$15,000. When Mary liquidates her 401(k) account, she gets to keep ALL of her \$30,000, instead of paying the \$4,000 capital gains tax that Bob has to pay. That's called tax-free growth, not tax-deferred growth, and that's why we encourage clients to maximize their savings through pre-tax retirement accounts.

As wonderful as that kind of tax-free growth is, there's another flavor in the form of Roth IRAs and Roth 401(k) accounts. A Roth account is different because it's funded with after-tax dollars, so you never enter into an investment partnership with the government. Let's assume Sally is in the same tax brackets as Bob and Mary, and like Bob she immediately pays \$5,000 of income tax on her \$15,000 bonus. But instead of taking the other \$10,000 and investing it in an after-tax account, she defers it into a



“...THERE ARE SEVERAL REASONS WHY THE ROTH AFTER-TAX APPROACH MIGHT BE SUPERIOR.”

Our Mission:

At RegentAtlantic Capital, we are committed to enriching the lives of our clients by delivering unsurpassed client satisfaction, peace of mind, and a full range of personalized wealth management services.

In this issue:

| | |
|--|-----|
| Kissing Your Partner Good-bye..... | 1-3 |
| Congratulations! | 2 |
| The Indefatigable Art Hyde3 | |
| Senior Seminar Series..... | 3 |
| Thank You to Our Clients..... | 3 |
| National Multiple Sclerosis Society..... | 4 |

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continued from page 1

Roth 401(k) account. If she puts her \$10,000 into the same stock and it grows to \$30,000, she can withdraw the \$30,000 and keep it all (as long as she's over age 59-1/2 and the Roth account has been in effect for five or more years). So Sally winds up in the same place as Mary, avoiding any \$4,000 capital gains tax on her \$20,000 of growth.

If Sally winds up in the same place as Mary, in that after-tax savings through a Roth account are equivalent to pre-tax savings through a traditional account, is there any reason to prefer one approach over the other? In fact, there are several reasons why the Roth after-tax approach might be superior:

- ◆ The minimum distribution rules that require withdrawals from all other retirement accounts to begin at age 70-1/2 don't apply to Roth IRAs. This means that 100% of your Roth IRA savings can continue growing tax-free until you choose to withdraw them, usually when all your other savings have been exhausted.

◆ All retirement savings funded by employer contributions are necessarily pre-tax partnerships with the government, so that withdrawals in your retirement years will be fully exposed to ordinary income tax. Having some of your savings in an after-tax Roth account is a way of creating "tax diversification" within your retirement portfolio, so that you hedge your bets vis-à-vis future tax law changes and your personal situation.

◆ In larger estates, after-tax Roth assets are much more efficient in reducing or avoiding federal and state death taxes than pre-tax retirement assets, because the available exemptions aren't being partially "wasted" on assets that will ultimately be paid to the government. In addition, with after-tax Roth assets the beneficiaries will avoid the nuisance and inefficiency associated with the "691(c) deduction" rules (ask your CPA).

Could saving on a Roth after-tax

basis be a bad idea? Yes, if someone's future marginal tax rates were going to be much lower than current tax rates. For example, if Sally was in the 40% marginal bracket today, but was going to be in the 25% bracket when she withdrew her retirement savings, she could do better with pre-tax rather than after-tax savings. If she chose after-tax savings, she'd pay \$6,000 in taxes on her \$15,000 bonus, put \$9,000 into that winning stock in her Roth 401(k) account, watch it grow to \$27,000, and withdraw the \$27,000 with no further tax. If she chose pre-tax savings, she'd defer the whole \$15,000 bonus into her pre-tax 401(k) account, watch it grow to \$45,000, and lose only \$11,250 to taxes upon withdrawal, leaving her with \$33,750. Roth after-tax savings and traditional pre-tax savings are equivalent ONLY when the saver's marginal tax brackets are the same in the contribution and withdrawal years.

Which brings us to the tantalizing opportunity to do a "Roth IRA conversion". That means electing to have your pre-tax IRA changed into an after-tax Roth IRA, which will require you to pay the income tax you'd owe if the pre-tax IRA was simply paid to you. Prior to 2010 an individual could convert a pre-tax IRA into a Roth IRA only in a year when the individual (plus his/her spouse if married) had adjusted gross income under \$100,000. In 2010 this income restriction will be lifted and all of us will be eligible to play the Roth IRA conversion game.

Let's go back to Mary, only this time we'll assume she did a tax-free rollover of her \$45,000 pre-tax 401(k) account into a traditional IRA. Her investment partnership with the government is still intact: in effect \$30,000 is hers to keep whenever she's willing to give the government their \$15,000. If she converts the rollover IRA into

a Roth IRA, and pays the \$15,000 of taxes with funds from some other after-tax account, she's taken \$15,000 of assets on which the future earnings would be subject to income and capital gains taxes and - Abracadabra! - changed them into \$15,000 of assets on which the future earnings will never be subject to income and capital gains taxes.

Is that too good to be true? Why wouldn't everyone kiss their government partner goodbye and convert all of their pre-tax retirement savings into Roth IRA assets? Actually, there are several reasons:

- ◆ You can't convert pre-tax savings that are still locked up in a retirement plan in connection with your current employment.
- ◆ A Roth conversion is less advantageous if you can't pay the resulting income taxes out of other after-tax savings.
- ◆ If you do a large Roth conversion in any one year, you may wind up paying a much higher marginal tax rate on the converted assets than you (or your beneficiaries) would have paid in future years

Doing a Roth IRA conversion either this year or next might - or might not - be highly advantageous to you and your beneficiaries. We will be happy to discuss this opportunity and provide appropriate scenario analysis to help clients decide whether they are candidates for this strategy. ◆

Thank you to our clients!

In the spring, we asked our clients to complete a survey on RegentAtlantic. The feedback has been enormously helpful to us. Thank you for taking the time to respond. Our friend, Al Mardirossian, won the drawing for a contribution to a favorite not-for-profit. Al chose the Scott M. Gonzalez Memorial Fund created in memory of State Trooper Gonzalez, who was killed in the line of duty. The fund provides scholarships and support to families of fallen New Jersey officers.

THE INDEFATIGABLE ART HYDE!



How many people do you know who simply can't stop working? How many people do you know who are absolutely passionate about what they do? Here's one such person: Art Hyde, Senior Director of Business Development at RegentAtlantic Capital. Art joined RegentAtlantic in the fall of 2008 after a very successful career, most notably being the founder of Beacon Trust, where he served as chairman, president and chief executive officer. An idea percolating in Art's mind back in the late '80's was to form a limited purpose trust company. Starting with nothing,

he and a group of friends raised \$2.5 million to launch Beacon Trust, a firm that had \$1.2 B in assets when he left. After graduating from The New York Law School, Art began a trust career with Morgan Guaranty Trust Company of New York and later was a Senior Trust Officer at Midlantic National Bank.

When asked what contributed to his success, Art said, "I have to believe in what I'm doing. And I believe that providing good financial advice to families is a very fulfilling career." Over the past year, Art has taken a strong interest in the "fine young people" at RegentAtlantic. He observed how the founders of the firm take a hands-on role in mentoring this next generation of financial professionals. When asked what has surprised him about RegentAtlantic, Art immediately talked about the "deep bench of talent" and the "atmosphere of cooperation."

Art serves on the boards of the Newark Day Center and the Reeves-Reed Arboretum. When Art is not at work in cultivating new clients for RegentAtlantic, he can be found enjoying one of his favorite activities - golf at Canoe Brook Country Club. Actually, our observation is that there is never a time when Art is not working!

Senior Seminar Series

Wealth Manager John Prokop invites you to a seminar series designed for persons either newly retired or who are facing retirement over the next 10 years. Space is limited. To attend, call Rachael Coleman at 973-425-8420, ext. 201 or rcoleman@regentatlantic.com.

Arrive at 5:45 PM for refreshments. Program begins at 6:00 PM!

- ◆ **November 11: "Turning back the clock - small changes you can make now!"** Speaker: Dr. Nancy Cotter, of Morristown Memorial and Overlook Hospitals
- ◆ **November 17: "How should my portfolio be constructed as I face retirement and how do I replace my paycheck?"** Speakers: Christopher J. Cordaro and William Knox RegentAtlantic Wealth Managers
- ◆ **December 2: "Getting My Act Together - Before My Final Act"** Speakers: RegentAtlantic Wealth Managers William Knox and Michael Steiner

Congratulations to Christina, Amanda, and Ann!



Congratulations to Analysts Amanda Newton, Christina Smith, and Ann Caruso who passed the CERTIFIED FINANCIAL PLANNER™ examination in July. The examination is 10 hours long and required many, many more hours of preparation. They look a lot happier now that their exam prep days are over!

NATIONAL MULTIPLE SCLEROSIS SOCIETY

by Martin M. Shenkman, Esq.



National
Multiple Sclerosis
Society

Every hour someone new is diagnosed with multiple sclerosis. The National Multiple Sclerosis Society is a collective of passionate individuals who want to do something about MS now.

Through its national office and 50-state network of chapters, the Society addresses the challenges of everyone affected by MS by funding research, advocating for change, and providing services that enhance the lives of people with MS and their caregivers. In 2008, the Society spent \$45 million on 440 research projects worldwide, and \$148 million on programs for more than one million people. Many of the Society's research projects also address issues common to other neurological diseases.

Being a volunteer driven organization, there are some 500,000 volunteers who help the Society fulfill its mission, many most visible during the Walk MS and Bike MS season. These events occur in hundreds of cities nationwide and foster MS communities sharing their stories to show policymakers why improving conditions for people with MS makes sense for everyone.

The Society's web site provides information and encouragement to the more than 400,000 people living with MS in the United States and 2 million worldwide. With the help of people like you, we can create a world free of MS. Please consider volunteering and sharing your special talents. The book, *Funding the Cure*, describes scores of charitable planning techniques you can use to help a friend or loved one living with MS and maximize your own tax and estate planning benefits, all while helping the National MS Society achieve its important goals. The book is available from www.demoshealth.com. All royalties go to the MS Society.

Join the movement by visiting www.nationalMSSociety.org or by calling Mary Milgrom at 1-800-923-7727 or email giftplanning@nmsss.org.



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