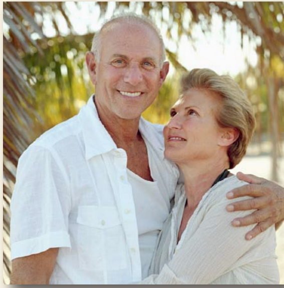
Understand critical steps for successful rollovers.

Learn about different types of IRAs and how they can help you achieve your retirement goals.

Discover best practices for leaving a legacy for loved ones through your IRA.

Build a Stronger Retirement with an IRA

IRAs can be a great tool –
if you understand how to use them



This guide was created by the financial professionals at American Financial.

The information contained in this booklet is designed to provide general information of the topic(s) covered. This material is intended for educational purposes only and is not intended to serve as the basis for any investment or purchasing decisions.

Based on IRS Circular 230, it is not intended to provide specific legal or tax advice and cannot be used to promote, market, or recommend any tax plan or arrangement. You are strongly encouraged to consult with your tax advisor or attorney.

You can use IRAs to build a solid foundation for your retirement

Most likely, Grampa relied on his pension (and his bank account) to fund his retirement. Mom and Dad may have grown up during the Depression, and counted on Social Security as a source of lifelong retirement income.

Today, however, you are pretty much on your own. Pensions are becoming more and more uncommon. And Social Security seems to be, well, insecure. More than ever before, you will be responsible for the cost of your retirement years. You will also have far greater control over how much you save, where you place those assets, and the degree of risk you are willing to undertake.

Consider your options carefully. The time you invest in learning about choices like IRAs can help you avoid costly errors and get the most benefit from the decisions you make.

Start by reviewing the information in this booklet. If you see a term you don't understand, circle or highlight it. Then schedule an appointment with your financial professional to go over what you've learned – and get answers to all your questions.

Look inside for these helpful strategies:

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2. Rollover to strengthen your IRA p4
3. Don't be intimidated by the rollover process p5
4. Take care when naming beneficiaries p6
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Assess your needs realistically

Perhaps the first mistake you can make in planning for your retirement is to underestimate its ultimate cost.

No one can predict the future. But overall, Americans are living longer. Life expectancies have trended upward in recent years, meaning your retirement could last years longer than your parents'.

If you remain healthy, you are likely to look forward to an active retirement filled with activities and adventures – many of which will cost money. If, on the other hand, your health fails, you could face medical costs (including the cost of hospitalization and long-term care) which may also have risen since your retirement began.

When you meet with a financial professional, you may be surprised at how much your retirement years could cost. Together, you can:

- Estimate how much retirement income you will need
- List your current resources for lifetime income
- Determine how many years that income will last
- Create a buffer for unexpected emergencies or opportunities
- Identify sources for additional income to maintain your comfort level

One cornerstone of your retirement funding strategy may be an individual retirement arrangement (IRA). Millions of Americans have used IRAs to help keep their retirement dreams within their reach. Hopefully, you can too.

You should be aware that tax laws have a significant impact on IRAs, and those tax laws change. You don't have to be an expert at tax law or finance, but you should be willing to consult one in order to get the maximum benefit from your IRA, and to avoid mistakes that could be expensive for you or your beneficiaries.

Rollover to strengthen your IRA

Years ago, it wasn't uncommon for someone to work for the same employer for 20, 30, even 40 years. The workplace has changed, however, and today's worker will likely change jobs several times. Many of those jobs may offer qualified retirement plans such as 401(k) plans.

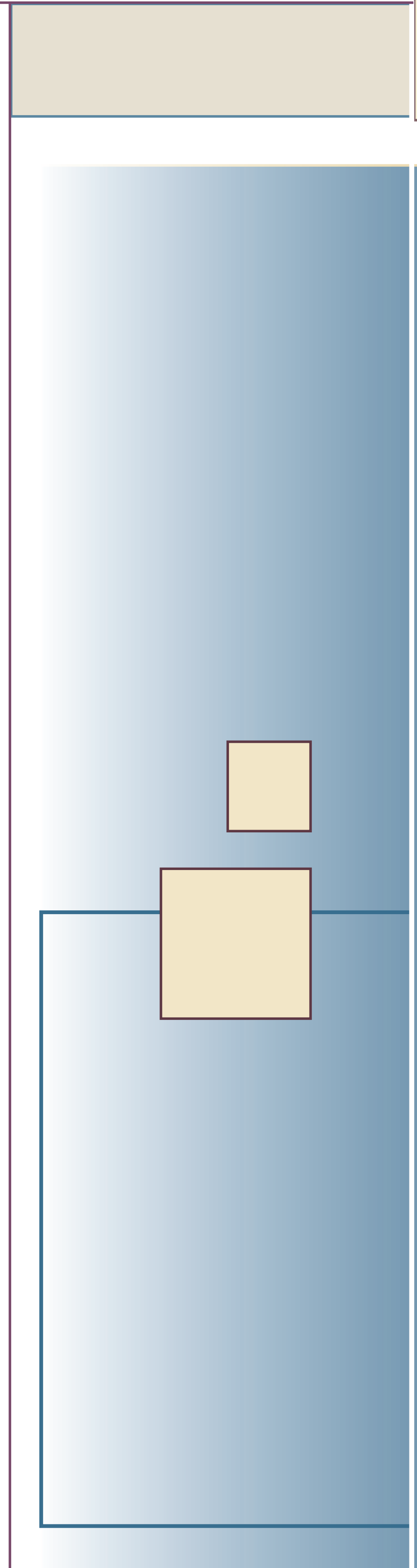
If you have recently lost your job, found a new one, or retired; you can roll the money accumulated in your previous employer's plan into an IRA. If done properly, this direct rollover is tax free. In addition to a direct rollover from a qualified retirement plan like a 401(k), money can be transferred from one traditional IRA to another traditional IRA.

You may be tempted to leave your money in your former company's plan. Perhaps you've been satisfied with your former plan's performance, and you're reluctant to change. You may have also heard assets held in a company-sponsored retirement plan enjoy greater protection from personal bankruptcy judgments and civil lawsuits.

Be aware this decision could impact how your heirs can receive those assets. When you place (or roll) that money into an IRA, your heirs will have the option to receive it in payments spread out over their life expectancies. Many company plan administrators don't want to be burdened with such an arrangement, so they may require an immediate, lump-sum payout.
The result: Years of tax-deferred growth can be dramatically reduced by the taxes payable on the lump-sum payout of your plan balance.

Even if this is not the case now, your former employer could be sold, which could result in new restrictions on how you can access your money in the future. Unless your company plan provides options you cannot get elsewhere, rolling that money into a new IRA may be the most prudent course of action. You should consult with a tax advisor or attorney regarding your specific situation as well as the fees associated with your plan and other options.

A word of caution: Be sure the money is directly rolled from the former plan's custodian to the custodian for your new IRA. Should you make the mistake of having the proceeds sent in a check made payable to you, you will be charged a 20% withholding tax. If you don't place the payout (including the 20% that was withheld) into a new IRA (or another eligible qualified retirement plan) within 60 days, you will required to pay income tax on the full amount of the distribution PLUS an IRS early withdrawal penalty if you are younger than age 59½.



Don't be intimidated by the rollover process

Admittedly, most of us don't roll money from a past employer's retirement plan into a new or existing IRA often. So the process can seem daunting. It shouldn't be. Keep in mind you will likely want to work with your team of financial professionals every step of the way.

Here's is a quick outline of the basic rollover process. We will assume you've decided to roll money from your company's retirement plan into a traditional IRA (rather than a Roth IRA, which we will discuss later).

You can roll your money from your company's plan to an existing IRA. For rollovers to an IRA you already own, contact your current account's custodian.

You can also open a new IRA and fund it with the proceeds from your company plan. Once you and your tax advisor agree this is the right decision for you, contact your financial professional (or a brokerage firm of your choice) to set up the new account.

Once you have made your decision, inform your former employer and provide the necessary account information. Your former employer will then roll the funds directly into your designated IRA. The transfer will likely be executed electronically. Another option is for your employer to send you a check MADE PAYABLE TO THE NEW CUSTODIAN RATHER THAN YOU.
You simply forward it to the custodian of your new IRA.

Since we are assuming the rolled-over funds flow to a traditional IRA, you will be required to take minimum distributions when you reach age 70½.

Take care when naming beneficiaries

Some IRA owners believe they don't need to name beneficiaries for their IRA(s). The reason is simple: they have executed a will. They believe their IRA proceeds will be distributed based on the terms and conditions set forth in their will.

In reality tax-deferred accounts provide for beneficiary designations that supersede those named in your will.

There is another important reason assets accumulated in an IRA should not pass through your will. If that should happen, those assets will pass to your estate. That means your IRA proceeds will become subject to probate. Additionally, those hard-earned IRA assets will be subject to creditors. Whatever is left after the probate process and creditors may be diminished by taxes.

You should also realize when an IRA is left to your estate its proceeds will generally be distributed shortly after you die. This is due to the fact that although an estate can receive your IRA's proceeds at death, it cannot be a designated beneficiary for your IRA. Your estate has no life expectancy over which payments can be calculated. The proceeds are therefore paid out immediately, ending any opportunity for continued tax-deferred growth. Also, estates are generally closed as quickly as possible.

Assets from an IRA should pass to the person(s) you name on your beneficiary designation form. With a properly designated beneficiary your IRA's proceeds can be distributed without the costs and delays of probate. The transfer would be handled confidentially as well, avoiding its inclusion in records that are accessible to everyone.

Regardless of whom you choose as your account's primary beneficiary, give careful thought to naming a contingent beneficiary as well. Many IRA owners are caught completely off-guard when their primary beneficiary dies unexpectedly. Simply having a contingent beneficiary in place can protect you from this unnecessary concern should the unthinkable occur.

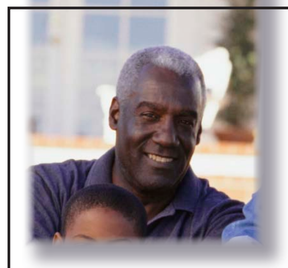
Let your IRA…

Let's presume you have multiple IRAs, one of which holds assets you intend to pass on when you die. When that happens your beneficiary will be required to satisfy the required minimum distribution rule. By using a stretch distribution strategy and carefully naming your beneficiaries, you can satisfy the required minimum distribution rules. This can help extend tax deferral for your beneficiary if they spread out distributions from the IRA over time.

A stretch distribution strategy can be a powerful way to pass on your wealth by minimizing the income tax your beneficiary will pay.

As the IRA owner, you could name your spouse as primary beneficiary to provide greater flexibility. If your spouse does not need your IRA's assets, you may designate a child or grandchild as beneficiary to receive distributions, based on their life expectancy, upon your death.

Obviously, we cannot address the benefits (and shortcomings) of diverse stretch strategies in a booklet like this. Here is a simplified example that shows a possible stretch strategy. Please note that the illustration below is not meant to represent all stretch distribution strategies.



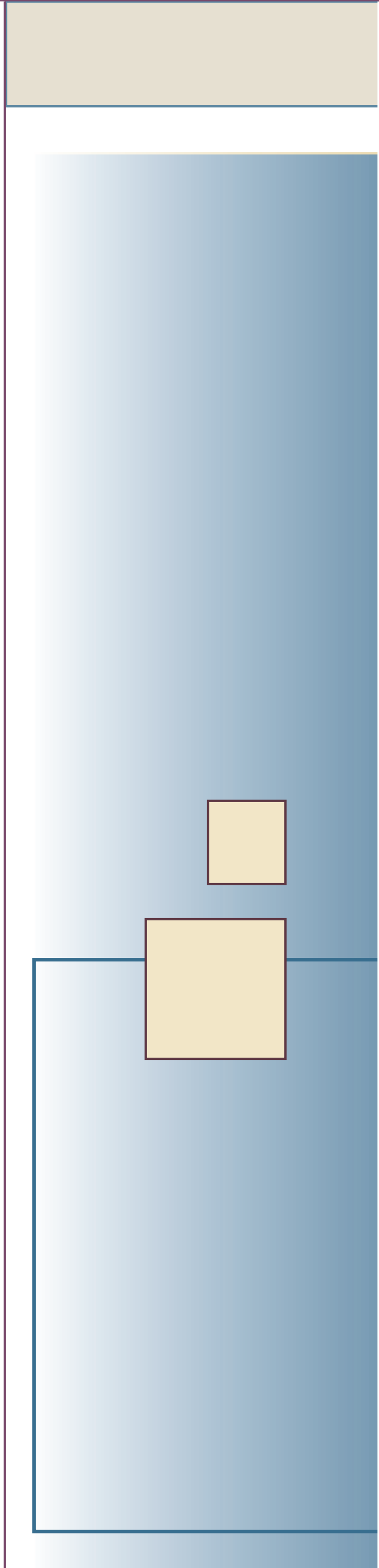
Al

- Opens an IRA
- He names his wife Beth as beneficiary
- Takes only RMD payments, once he reaches age 70½

Beth, his wife

- Rolls the IRA under her name when husband Al dies
- Designates daughter Sarah as beneficiary
- Takes only RMD payments after age 70½

… stretch into the future



As you refer to our stretch distribution timeline, you will note payments can extend over many years. Throughout the "lifetime" of the IRA, its value will be diminished by the payments taken by each of the hypothetical individuals shown.

A well conceived stretch strategy must assure that the IRA was sufficiently funded to retain assets throughout the entire stretch distribution period. Otherwise, the IRA can simply run out of money. Of course, a properly structured stretch strategy can continue to deliver tax-deferred potential growth, which can offset required minimum distributions.

In reality creating a successful stretch distribution strategy must be done carefully to maximize your IRA's benefit to your beneficiaries. Although you may wish to designate your spouse as beneficiary, it may be more prudent to name your child or grandchild. If that is the case, you must decide whether to designate a minor as beneficiary, which could require you to name a guardian for the minor. You can also choose another option such as establishing a Uniform Transfer to Minors Act (UTMA) account.

To help assure your stretch strategy is successful, be sure to talk to your tax advisor or accountant.

Please note: A stretch distribution strategy is most effective when individuals can afford to minimize IRA distributions during their lifetime and are able to pass remaining assets on to future generations. For traditional IRAs, keep in mind that you must begin taking required minimum distributions by April 1st of the year after you reach age 70½. Changes in tax law, the impact of inflation, costs, and risks of underlying funding vehicles may have a significant impact on the long-term value of your IRA.

Sarah, their daughter

- Is 57 when Beth dies; she receives her mom's remaining IRA proceeds
- Elects to receive the proceeds in payments (which must be based on her life expectancy of 86 years)
- Takes required payments until she dies at age 77

Liz, Al and Beth's granddaughter

- Can continue to receive payments until the date of Sarah's life expectancy is reached

Review your beneficiary designations periodically

Earlier we cautioned about the need to take care in naming a designated (and contingent) beneficiary.

The pro-active attitude you should have when naming a beneficiary should continue throughout the life of the IRA. Talk to your financial professional about periodic reviews of your beneficiary designation(s). And make whatever changes may become necessary to keep your designations up to date.

It seems obvious, but people and relationships can change dramatically as the years pass. Think about the changes your family has seen over the past 10, 20, or even 30 years. Who could have predicted them?

Fortunately, you don't have to. Just remember to review your IRA's beneficiary designations periodically. Then rest easy.

One final suggestion: Make certain your beneficiaries know exactly where your IRA beneficiary forms are stored. Although your financial institution will have a copy, your beneficiaries may have no idea where you conduct your personal financial transactions. If your designated beneficiaries lose track of the form, they could lose their standing as inheritors of your IRA.

Explore the benefits of a beneficial IRA

We've already discussed the ways a stretch distribution strategy may extend an IRA's tax deferral to your beneficiaries. Even if a stretch strategy does not fit into your plans, you should take steps to maximize the tax advantages of your IRA at your death.

When the original IRA owner dies, the beneficiary can keep the IRA "alive" as a beneficial (or decedent) IRA. The title of the new IRA must demonstrate that the IRA will be a beneficial IRA going forward. A sample title could be "Allison R. Dudley as beneficiary of Richard P. Dudley, deceased."

The beneficiary can select from a number of distribution options. The choices available will be based upon:

- Whether the beneficiary is the spouse of the original IRA owner, and
- Whether the owner passes away before or after April 1st of the year after attaining age 70½

If the beneficiary is the IRA owner's spouse, they will also have an option to roll the decedent's IRA in their name (rather than maintain it as a beneficial IRA). This will allow the new IRA owner to designate a new beneficiary. It will also impact the new owner's treatment regarding required minimum distributions.

Make sure your beneficiary is aware of the options they have. It may be prudent to schedule a meeting with your beneficiaries, your financial professional, and your tax advisor to agree on a strategy that will derive maximum benefit from your IRA when you pass away.

Weigh the benefits of a Roth IRA

Throughout this guide, we have repeatedly referred to "traditional IRAs." But what about their "nontraditional" counterpart, the Roth IRA? The basic difference is quite easy to grasp.

You can pay the IRS now (and fund a Roth IRA with after-tax dollars). Or you can pay the IRS later (by placing tax-qualified money in a traditional IRA).

If you are eligible for a deductible contribution and choose a traditional IRA, you will defer paying taxes on both your initial principal and any credited interest. If you are eligible for and choose a Roth IRA, your after-tax dollars can also benefit from tax-deferred growth – as long as you abide by the IRS rules for qualified Roth distributions. For traditional IRAs, those taxes are deferred until you begin to receive your IRA's value in distributions, including the minimum distributions required once you reach age 70½. Any money you receive will then be subject to taxation as ordinary income. There will be an additional 10% penalty if you receive the funds before you reach age 59½.

You will want to wait until your first Roth IRA reaches its 5th anniversary. Once you have held your first Roth IRA for five years, your distribution from any Roth IRA is income-tax free if any one of these qualifying events occurs:

- Owner is age 59½ or older
- Death of owner
- Owner becomes disabled
- Owner receives $10,000 or less for a first-time home purchase

An important added benefit is the fact that **qualified Roth distributions don't increase your adjusted gross income (AGI)**. This matters because:

- A lower AGI can shield more of your future Social Security benefits from taxation
- It can also impact the amount you can deduct for medical expenses
- The levels at which personal exemptions and itemized deductions phase out are based on your adjusted gross income

Qualified distributions from a Roth IRA can be a win-win situation. So why are some people so intimidated by Roth IRAs?

Complexity is the price of Roth IRA flexibility

We've tried to keep our explanation simple by focusing on ways to take qualified (meaning income tax-free) distributions of Roth IRA funds. If you don't meet the requirements, you could expect you will have to pay some amount of income tax. But you may not have to.

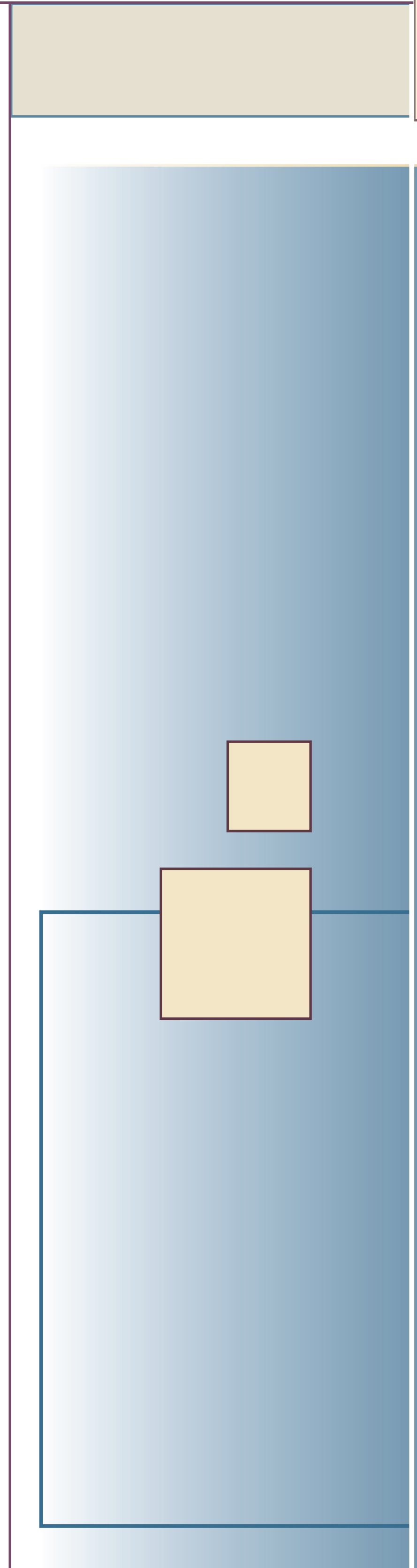
Whether you funded your Roth IRA with annual contributions or converted a traditional IRA to a Roth, you paid income taxes on the money you placed in it. You simply haven't paid taxes on the interest or growth you've achieved. So the IRS has created "ordering rules" to clarify the order in which nonqualified distributions can come out of a Roth IRA. The ordering rules for money placed in a new Roth IRA differ from those that govern conversions from traditional IRAs and direct rollovers from qualified plans to Roth IRAs.

A guide like this cannot provide a comprehensive explanation of IRS ordering rules. Likewise, it cannot adequately address topics like Roth IRA:

- Conversions
- Reconversions
- Direct rollovers from qualified plans
- Recharacterizations, and more

So if someday you are considering a Roth IRA – or if you already own a Roth and want to receive a distribution from it – remember to consult with your tax advisor or attorney. They'll help determine the right strategy for you. And for now, turn the page.

It is generally preferable that you have funds to pay the taxes due upon conversion from funds outside of your IRA. If you elect to take a distribution from your IRA to pay the conversion taxes, please keep in mind the potential consequences, such as an assessment of product surrender charges or additional IRS penalties for premature distributions. You should consult with your tax advisor to discuss which payment option is appropriate for your personal tax situation prior to any discussions with an agent or representative.



Maybe the best choice is not choosing

By now you may be thinking a traditional IRA could be your best option. Or perhaps you feel it's time you considered a Roth IRA. Or maybe you can't choose either because you're suffering from information overload.

Relax. We're talking about your retirement savings strategy, not a trip to Europe.

When you are restricted to a single suitcase, you have to make a number of decisions. Heels, flats, or flip flops? A sportcoat or a sweater vest? The gray slacks or another pair of khakis?

This is not the case when the discussion centers around your retirement portfolio. Unlike your suitcase, your portfolio can be expanded and adjusted based on the informed decisions you make today – and years from now.

So don't be afraid to settle on a traditional IRA for the benefits it provides, or a Roth IRA for its advantages, or both. You may find your decision to fund AN individual retirement account is far more important than WHICH type of IRA you choose.

Take the next step

We hope this guide has given you a better understanding about some of the key features and benefits individual retirement accounts can provide. We trust you have gained valuable insights regarding:

- Naming and updating beneficiaries
- Rolling your employer's qualified plan to an IRA
- Stretching your IRA to extend its benefits to future generations
- What mistakes can you avoid to maximize the value of your IRA

Before you open an IRA, you should have a thorough discussion of your current financial situation and your future retirement (and legacy) goals. It's a conversation that should include your tax advisor or attorney, along with the financial professional who made this booklet available to you. For your convenience, you'll find their contact information on the next page.

As we've mentioned previously, this booklet was created to give you a basic understanding of IRAs. It cannot provide insight as to what type of IRA is ultimately a suitable choice for you, or what strategies will best protect you from paying unnecessary taxes. So you should include your tax advisor, accountant, lawyer, or estate planning specialist in the discussion prior to making your decision.

Photo of rep.

Rep Bio

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