

Tax-deferred  
investing to help  
achieve your  
retirement goals



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Starting to put money away for retirement early in your adult life is a smart and powerful way to help you become financially secure when it is time to retire. While almost any form of savings is better than not saving at all, you want to maximize the impact of your efforts to give yourself the best chance of achieving the lifestyle you want for your retirement years. One of the most effective tools in the retirement-toolbox is tax deferral,\* and this eBook explains some helpful ways to incorporate different approaches into your overall investing for retirement plan.

Why is tax deferral so useful and important in planning for retirement? Simply put, by postponing tax payments on your investment income, you keep more of your money invested for the long haul. Annuities are tax-deferred investment products specifically designed for retirement. One of the key advantages of including an annuity as part of your retirement planning strategy is that you pay no taxes on your investment earnings until you choose to start receiving income from the annuity, any time after you reach the age of 59½ and typically after you retire. This allows 100% of the investment returns you generate to keep working for you, for 10, 20, even 30 years (or longer). That's a big advantage over paying taxes out of those returns every year.

#### **What is an Annuity?**

Annuities are long-term, tax-deferred vehicles designed for retirement. Variable annuities involve investment risks and may lose value. Earnings are taxable as ordinary income when distributed and may be subject to a 10% additional tax if withdrawn before age 59½.

\* Tax deferral offers no additional value if an annuity is used to fund a qualified plan, such as a 401(k) or IRA. It also may not be available if the annuity is owned by a "non-natural person" such as a corporation or certain types of trusts.

Understanding the impact: The Rule of 72

One way to think about how postponing taxes helps your retirement savings to grow is something called the “Rule of 72.” The [Rule of 72](#)<sup>1</sup> is a quick way to estimate how long it would take an amount of money to double when it is invested at a specified rate of return. To use this rule, simply divide the number 72 by the investment’s rate of return – the result is the number of years it will take for that investment to double.

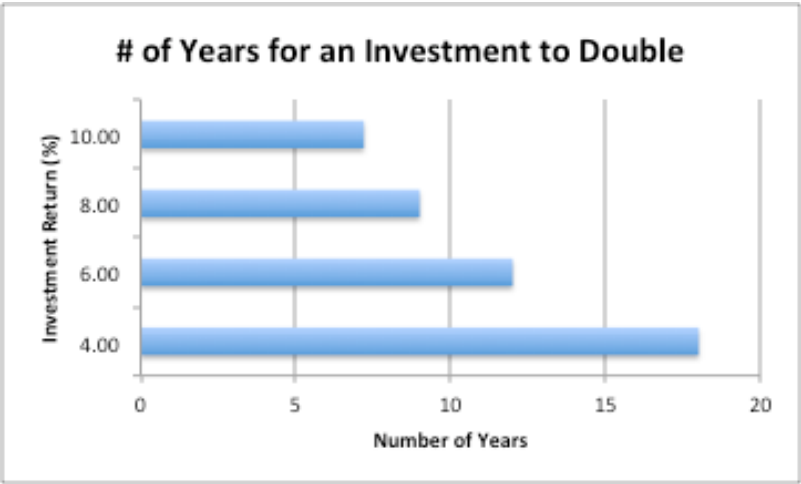
For example, if your rate of return is 4%, the amount of money you invest will double in  $72 \div 4 = 18$  years. However, if you can earn a 6% return, your money doubles in just 12 years ( $= 72 \div 6$ ), and so on. The higher the return, the less time it takes for your savings to double.

However, if you have to pay taxes on your investment earnings you cannot use the Rule of 72; it takes longer for your money to double. Why? Because some of the money that would have stayed in the account, earning more of that rate of return year after year, is taken out to pay taxes. For investors in a 24% tax bracket, it would take an additional five years (approximately) for an investment to double. This can make a big difference in the amount of savings you ultimately accumulate to help meet your lifestyle goals in retirement.

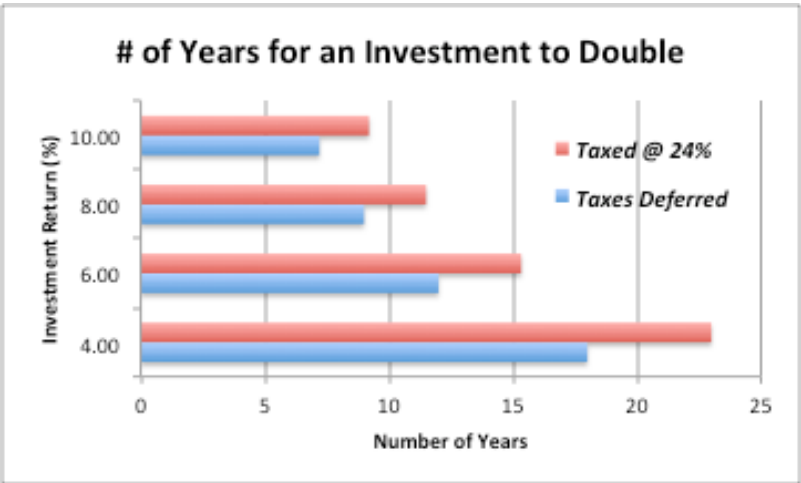
Although most of us probably don’t think about saving and investing in terms of how long it will take for our money to double, it is a good way to see the “dampening” effect of taxes on investment results and how paying or deferring taxes can impact how quickly our savings grow.

Let’s imagine you are currently 50 years old and have saved \$100,000 outside of your 401K (or IRA), in a taxable savings account. You decide you want to keep half of these savings in the taxable savings account, to cover big purchases and unexpected expenses. You decide to invest the other half for the long-term, to generate future income that will help you live the lifestyle you want in retirement. An annuity allows you to defer paying taxes on your investment returns until that time in the future when you start withdrawing money, after age 59 ½ or later, depending upon your needs. The ability to defer tax payments, possibly for many years, makes a big difference in the amount of money you can save compared to a taxable investment account where you must pay taxes on your earnings every year.

Assume you invest half of the money, \$50,000, in a tax-deferred account. For the purpose of this example, we’ll assume it produces a return of 6% per year. The Rule of 72 tells us that \$50,000 will turn into \$100,000 by the time you are 62, when you might be ready to retire. Assuming you are 40 years old, \$50,000 invested today would give you \$200,000 by age 64, doubling twice over that period. Let’s assume the money in a taxable savings account also earns a 6% return per year, and that you are in the 24% tax bracket. Assume the \$200,000 is withdrawn from the account over the next four years. If the saver is in a 20% tax bracket in retirement and continues to earn a 6% return on the amount remaining in the account after each withdrawal, he would keep over \$185,000 after taxes. Without the ability to defer taxes, a 50 year old would have to wait until age 67 to see that money double, compared to age 62 for the tax-deferred account. A 40-year old would be 74 before that \$50,000 turned into \$200,000, compared to age 64 with the tax-deferred account.



Note: This chart is for illustrative purposes only and does not represent any specific investments.



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This comparison is intended to show that tax-deferred savings increase much faster than non-tax-deferred savings. Of course, once you start withdrawing money from the tax-deferred account, you will pay taxes on those withdrawals. Your tax bracket at that time will ultimately determine how much of those savings you ultimately keep. You may be young and early in your career, in your 40s or already in your 50s. Whatever your stage in life, whether you have only modest savings or have accumulated a big investment portfolio, whether you work for a company, own your own business, or are staying home to raise your children, we all have one thing in common: we want a comfortable retirement. And the earlier we start saving for it, the more we can take advantage of the benefits of tax deferral.

### **Annuities: a strong option for tax deferral**

As you start to appreciate how an annuity's tax advantage can help improve your ability to achieve your retirement goals, it's important to remember that annuities are not a "one size fits all" approach to saving for retirement. Variable annuities allow you to invest in just about any mix of investment types, giving you exposure to various markets, both in the U.S. and globally, just as you would when using non-tax- deferred investing<sup>5</sup>. You decide how your money is allocated across different types of investments: stock mutual funds; ETFs that invest in stocks, including those that invest globally; fixed-income assets securities, ranging from more conservative U.S. Treasuries to riskier but potentially more rewarding High Yield corporate bonds; and even alternative investments. You choose the tradeoff that is right for you, between lower risk/lower returns and higher risk/higher potential returns.

This flexibility allows you to create an optimal approach to tax-deferred investing across your entire retirement portfolio, complementing the often-limited choices you have through a 401(k) plan. For example, if your 401(k) plan offers a fund that invests in the broad U.S. stock market but does not offer an emerging market stock fund that you would like to hold, you may be able to use your variable annuity to gain access to that type of investment and retain the advantages of deferring taxes described earlier.

A variable annuity can also be used to help reduce the tax liability generated through your taxable investment accounts. Variable annuities allow you to invest in a mix of products or "asset classes" (stocks and bonds, for example) that offer exposure to various types of investments. You choose the trade-off between risk and future potential return offered by these various investment products that is right for you. This arrangement opens up the flexibility to focus your taxable brokerage account funds on investments that gain exposure to the stock market (assuming that's what you want) in ways that generate much lower annual income, such as many ETFs that track various stock market indexes.

This is the notion of "asset location" mentioned in [Tax Advantages of Annuities: Understanding the benefits for you and your family](#). If you use a variable annuity to hold the types of investments that generate a relatively high amount of taxable income, and use your taxable brokerage account to buy investments that generate a relatively low amount of taxable income, then you defer paying taxes on the majority of your investment income while still achieving the overall mix of investments that is right for you.

Another advantage of tax-deferred investing is that it can simplify year-end tax preparation. The rules for identifying the original cost of shares of stocks or funds that were sold during the year, which then determines the gain (or loss) on the sale, are complicated. Instead of having to keep track of every purchase and sale in your portfolio for your tax return, when you do start receiving income from your annuity and owe taxes on that income, you receive a simple report that saves you time and aggravation as that April 15 tax date approaches.

### **Pursuing a vibrant life in retirement**

At some point, you may realize that through discipline and planning ahead, you are on track to build a nest egg for a comfortable retirement. What a great feeling! But that doesn't mean you no longer need, or should care about, the tax advantages and other benefits for you and your heirs that annuities can offer. For example, consider a couple in their early 50s, roughly 10 years from retirement. Both have contributed the maximum amount to their 401(k) plans at work for many years, and most of that money is invested in various U.S. stock mutual funds. They have regularly contributed to their children's college savings plans and have a decent amount of savings in a taxable brokerage account. They believe the combination of their 401(k)s, Social Security benefits and additional savings will provide them with a good income when they retire, especially since their home mortgage will be paid off in about 10 more years. They should feel good about the healthy financial habits they have maintained over the years.



When they retire, this hypothetical couple will want to travel and plan to be active as long as possible. They are in good health and have a good chance of living a long time after they stop working. They have frequently heard that people underestimate what their living expenses will be after their retirement, especially medical expenses in later years. Even though they feel the money in their combined savings accounts plus Social Security will most likely cover these expected expenses, it would give them extra peace of mind to have a source of income that will last them as long as they live – and that’s exactly what an annuity can do. An annuity can be structured to provide lifetime income – even if you live to be 90+ ([which more people are doing](#)).<sup>2†</sup>

If you have this comfortable retirement outlook, you could buy an annuity at age 50 and plan to use other income sources (such as 401Ks and Social Security) to meet your expenses until age 75. By delaying your annuity payouts for 25 years, you defer taxes for that entire time. Using the Rule of 72, you can estimate how much your assets might grow. You might then choose to receive payouts from the annuity over a 20-year period, which would last until you are 95!

You can also choose to have your annuity include a potential benefit<sup>‡</sup> for your heirs. Your beneficiaries may be able to stretch out the remaining distributions in a way that avoids a big tax hit for them. Or, by choosing to take annuity income over a shorter period, you could have extra cash on hand to help with priorities such as replacing a roof, paying for long-term care not covered by Medicare, contributing to a grandchild’s education, or making donations to charity.

† Guarantees are backed by the claims-paying ability of the issuing insurance company

‡ Optional benefits are available for an extra charge in addition to the ongoing fees and expenses of the variable annuity.





A photograph of an older couple on a boat. The woman, with short blonde hair, is smiling broadly and looking towards the man. The man, wearing a blue and white striped shirt, is partially visible on the right side of the frame. The background shows the blue water of the sea under a bright sky.

## As the old saying goes, in this world nothing is certain but death and taxes.

Annuities can't do much about death, but they can help you to delay taxes as long as possible. No matter which structure you choose, all annuities offer the option of letting you defer taxes on your investment earnings, and that can translate into a big advantage for you and your family.

We encourage you to work with your financial advisor to help you come up with an advantageous tax strategy—one that meets your financial needs, wants and goals for the future.



<sup>1</sup> Investopedia, "What is the Rule of 72", Jan 2018

<sup>2</sup> US Census Bureau, "Census Bureau Releases Comprehensive Analysis of Fast-Growing 90-and-Older Population", Nov 2011

**Before investing, investors should carefully consider the investment objectives, risks, charges and expenses of the variable annuity and its underlying investment options. The current contract prospectus and underlying fund prospectuses, which are contained in the same document, provide this and other important information. Please contact your Internal Wholesaler to obtain the prospectuses. Please read the prospectuses carefully before investing or sending money.**

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