

Making Lemonade Out Of Lemons

This month I wanted to tell you about a recent case I worked on that had an interesting twist to it.

PLEASE NOTE THAT I HAVE CHANGED THE NAMES AND CIRCUMSTANCES SLIGHTLY TO PROTECT THE PRIVACY OF THE CLIENT.

I met John a couple of months ago. He responded to Pamela Yellen's ezine newsletter asking to talk to an authorized BOY advisor about his situation.

John owns a small business that is coming back to life after a very tough 2008. John was forced to lay off a full time employee and ran up a lot of business debt while he set in motion the 180 degree turn around that he has seen in his business in 2009.

He is very concerned about the debt because of the outrageous interest rates he is currently being charged. He was forced to use his credit cards to finance the business turnaround because no bank would give him the time of day. He has seen the interest rates balloon to over 20% and even over 30% on one of these cards.

After handing out credit cards like candy, these card companies are now squeezing the poor souls who were forced to use their cards. This is the kind of deal I would expect from Tony Soprano. No wonder an attorney friend of mine calls credit card companies "dope peddlers"!

By the way, helping people deal with credit card balances and high interest rates is part of a BOY analysis, so it does not cost a dime and there is no obligation to get my 2 cents on the best way to deal with your situation.

Now let's get back to our story.

When I talked to John and his wife, Agnes, I found out that she was even more concerned about the debt than him. I also found out that they had plenty of money in their IRA's to pay off the business debt, but little other money available in savings. When we talked about their goals and concerns, they told me that they now wish they had never put the much money into the IRA's. They said they fell in love with the tax deduction and never put any money into regular savings because the returns were so low. They also talked about how they wished they had saved more money over the years.

For too many people, IRA's and 401k's are the only real back up money they have. When something happens, they are forced to take money out of these accounts and pay income taxes and penalty.

I say, "Forget about the tax deduction!"

For 95% of the people I talk to, the tax deduction amounts to less than 15% on the money they put in. In return, their money is tied up in knots for a long time and subject to unknown taxation in the future.

It is much more important to have the money available in a place where there will be no future taxation of it if you can pay a reasonable amount of tax on it today, like with BOY plans.

So here's what happened with John and Agnes.

Because of John's business problems, his income in 2009 will be a record low for him. This has created an opportunity for them to take money out of their IRA with a very low tax consequence even though they had to pay a penalty. We asked their accountant to estimate the taxes that would be due if enough money was taken out of the IRA accounts to pay off the credit cards. In their case, because of their low income situation, the total federal and state income tax due would be 20%, including the penalty.

John and Agnes thought that was a no brainer decision. They took the money out and loaned it to the business. They also did what their accountant advised and set up a formal promissory note with the business that has a market interest rate and reasonable payment terms. Now the business will make loan repayments to them every month instead of paying the credit card companies AND still be able to deduct the interest paid.

Guess what they are going to do with that loan repayment money every month?

They are starting a BOY plan so they can start to build up their back up money on a systematic basis and create a nice nest egg within a few years.

They never want to get hooked on credit card dope again.

Now they will start to have liquid available loan value in their BOY plan. They will also have flexibility in paying the premium on the BOY plan in case the business has to reduce or skip loan repayments along the way.

I love it when a plan comes together. While I can't promise this same result in every case, I will not know what I can do for you unless you raise your hand and ask me to take a look at your situation.

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