



## AMERICAN FINANCIAL ADVISORS, LLC

### A Worthwhile Letter to Your Children/Heirs

**NOTE:** Below is a letter we edited from Michael Jones, member of the CPA firm, Thompson Jones LLP in Monterey, CA. We customized the original for our clients. It is an important letter to consider including in your files with your Will. Your children/heirs will “thank you”, for including this type of information – thus saving them from classic mistakes many families make when a close family member passes away. We are including it in this mailing since many of your children will be home, visiting or calling -- over the holidays. “Money” is often taboo – and not discussed in far too many families -- which is why missteps occur and thousands of dollars are handed over to Uncle Sam unnecessarily every year. Our job is to keep you from being included in that number.

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Dear Children/Heirs:

As you may have learned by now, you have inherited my IRA(s) in equal shares. The IRA you have inherited is a legal tax shelter that can be kept as a tax deferred investment account well into the future.

First, I’ll discuss the golden rule of maximizing the value of your inherited IRA and the requirements to take withdrawals. Then I’ll tell you what you must do now -- since I am no longer here to help.

#### **THE GOLDEN RULE:**

The golden rule of maximizing the value of your inherited IRA is:

*Every year, withdraw only what may be required, and no more.*

Here's why:

You produce the greatest possible tax-sheltered earnings and growth on the IRA by leaving the most money invested for the longest time possible. Keeping the maximum amount compounding inside the IRA is the course of action likely to produce the greatest value.

If you invest wisely and leave your investments in the IRA long enough, you have the best chance to cover all the taxes you would pay by withdrawing the entire IRA now.

On the other hand, each dollar you withdraw now will cost you income taxes. The more you take out, the higher the income taxes you pay. Those rates increase as your taxable income rises. When you take an IRA withdrawal you don't have to, you voluntarily end your tax-sheltered investing opportunities. Thus, you pay more income taxes than you would otherwise owe. That enriches Uncle Sam - at *your* expense. Every dollar taken out of your inherited IRA can never be put back in - *even* if taken by mistake.

#### **WHAT YOU ARE REQUIRED TO TAKE OUT**

Tax laws impose annual "required minimum distributions" (RMD). IRA owners generally must take them during their lifetime – or after you inherit an IRA.

Required minimum distributions are determined by dividing the account balance by your life expectancy in years. For example, \$100,000 divided by 25 years = \$4,000 per year. Your actual amount may vary depending upon your age of withdrawal and life expectancy factor when distributed.

A hefty federal tax penalty applies when you fail to withdraw the required minimum distributions. The penalty is 50 percent of the amount that should have been withdrawn. That penalty applies - *in addition* to any normal income tax due on the withdrawal.

It is possible I had not yet taken the distribution required during the year of my death. In that case, you must take that distribution by December 31 of the year of my death and pay any income taxes due on that distribution.

Starting with the year after my death, distributions are then based on your life expectancy, but only if you set up an inherited IRA during the time allotted by the IRS.

On the other hand, if you fail to divide up the account by December 31 of the year AFTER my death -- then all of you must use the shortest life expectancy which would be the oldest child. The rules that permit division of the account by December 31 of the year AFTER the IRA owner's death are provided in the income tax regulations. If anyone questions this, have them look up Income Tax Regulation Section 1.401(a)(9)-7, Question & Answer 2(b).

### **WHAT YOU MUST DO NOW**

First, don't do ANYTHING or TAKE ANY MONEY until you've discussed your proposed actions with my financial advisor. They understand these rules and a mistake can be unnecessarily costly.

For a copy of my beneficiary designation and instructions on how to claim your share of my IRA, contact American Financial Advisors, LLC (AFA) toll free at (888) 413-9080.

Right now, the IRA is held in my name. Each of you must set up an **Inherited IRA** for your share of my IRA. Your Inherited IRA account must be titled in my name as the deceased IRA owner and held for your benefit as beneficiary. You may each set up your Inherited IRA with the IRA custodian that I used, or you may use any other qualified IRA custodian. (Schwab, Fidelity, Merrill Lynch, Wachovia, etc.)

However, if you decide to use a different custodian, make sure the account is moved in a DIRECT TRANSFER, trustee-to-trustee, since you are NOT permitted to do a Rollover IRA.

Here's how to divide up the account. It would be preferable to divide up the account by December 31 of the year of my death.

But, as I stated earlier, it can be done by December 31 of the year after my death. If you wait beyond December 31 of the year after my death, you must use the life expectancy of the oldest child who is a beneficiary. Larger required minimum distributions would deplete the IRA sooner. This is not the best choice.

If you act in time, you can use your *own* life expectancies based on your age attained in the year after my death. This is much better.

After establishing the Inherited IRA account for each of you, my IRA can be divided and transferred to each of those accounts.

### **ASK IN WRITING - FOR A DIRECT TRANSFER, NOT A ROLLOVER**

**DO NOT ASK FOR A ROLLOVER BECAUSE A PERSON WHO INHERITS AN IRA CAN NEVER DO A ROLLOVER. ONLY A SURVIVING SPOUSE HAS THIS OPTION.**

These rules can be complex so please check with nice people at AFA before you make any decisions.

*Your Loving Father/Mother*

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