SCARY MATH:
Where are taxes headed and what are you going to do about it?

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Most people don't like to think about taxes, but smart people will take the time to ask themselves: Am I prepared for the future? Have I evaluated tax brackets? Have I done the math? Have I prepared my distribution strategy accordingly? What will happen when I die?

Many people are mistaken when they assume they know which tax bracket they can expect when they reach age 60 and age 70. Do you think your tax bracket will be higher or lower than it is today? Consider the following data.

In order to understand where our tax dollars go, become familiar with the three categories of our federal budget:

1. ***Mandatory spending:*** This is the federal funding that continues each year without Congress having to approve it. Social Security, Medicare, and Medicaid comprise almost 70 percent of all mandatory spending. Consider these facts.

    - Half of the 70 million baby boomers in the US today are totally dependent on government programs.
    - By 2035, 80% of the projected growth in federal spending as a share of GDP (other than interest payments on the debt) will come from growth in spending on the three largest entitlement programs: Medicare, Medicaid, and Social Security.
    - Unfunded entitlement programs approximate $53 Trillion.
    - According to the Congress Budgetary Office, in 2020, 47% of our Federal Budget will be comprised of Social Security, Medicare / Medicaid.
    - Funding for Social Security benefits is projected to run out in 2017.

2. ***Discretionary spending***: funding that Congress must re-appropriate by vote each year.

3. ***Interest Payments***: the annual costs associated with the federal debt. As the federal government runs deficits and borrows money, it builds up an accumulated level of debt. The government, just as any other borrower, has to pay interest on that debt.

    - The National debt as this article is written is $18 Trillion.
    - Projections indicate that in 2014 our federal deficit will be greater than our annual inflow.
    - Our national debt approximates to increase to nearly 100% of GDP by 2020.

- Each year since 1969, Congress has overspent its income. The Treasury Department has to borrow money to meet Congress's appropriations. As taxpayers, we pay a staggering amount of interest on that huge debt. And now the Treasury is having trouble finding lenders! Soon the interest payment on your loan is bigger than any other item in your budget. Eventually, all you can do is pay the interest payment, and you don't have any money left over for anything else.

Switching gears now from your government's money to your household's money, let's turn to your personal wealth. There are four buckets of wealth:

1. Pre-tax: this refers to contributions made before paying income taxes, such as with a deductible IRA, SEP, 401k, PSP, etc.
2. After-tax: this refers to contributions or investments made after paying income taxes such as with a saving account, CD, mutual fund, etc.
3. Tax-deferred: this is income on which the payment of taxes is deferred until a later time, such as the unrecognized growth of an investment, or build-up of cash value of an annuity.
4. Tax Free: this is income on which no tax liability exists, such as qualified distributions from a Roth IRA, and other non-qualified assets such as properly structured withdrawals from life insurance. Note: Income from municipal bonds may be both federal and state income tax free, depending on the type. However while the income is income tax-free it may be included in the Alternative Minimum Tax (AMT) calculation.

One example of the effect of taxation on your personal wealth is a common scenario. One common sense rule of investing is to buy low, hold, and sell high, right? If you had invested $10 into the large cap index in 1958; that $10 would have grown to $1100 in 2008. But after federal income taxes, that value would have shrunk 75% to $303. And that doesn't even include state, local, and consumption taxes. Are you evaluating net rate of return or gross rate of return? Are your current strategies designed to save you taxes or are you merely delaying the tax burden? Will unexpected taxation affect your future standard of living? The wealth you may be counting on is wealth the government is counting on as well. Depending on which bucket of wealth holds the majority of your dollars, you may not wind up in the tax bracket you expected! Forward thinkers will seek out strategies to insulate themselves and their heirs from the massive tax liability facing all Americans.

Does the past offer us any insight into the future? The Federal Income Tax in its present form started in 1913 with a top tax bracket of 7% on income over $500,000. The highest tax bracket peaked in 1952-1953 at 92% tax on income over $400,000. The top tax bracket today starts with annual household income over $373,651 and is taxed at 35%. What's different now? Our national budget will force the hand of government once again. Though we cannot predict the exact actions of our future government, we can act now on solid data, strategies, and foresight to minimize the impact to our personal wealth.

It's not all bad news: you are not powerless! Visit www.usdebtclock.org or visit with your trusted financial advisor to seek solutions to these urgent and imminent problems. Actions taken now can help you to achieve the retirement and legacy you are working so hard to attain. You can enjoy the fruits of your labor by shielding your crops from the storms. Just don't wait until the sky darkens.