Time-Sensitive Research for **Project to Restore America** Members

The Most Important Thing You Need to Know about Taxmageddon

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The Most Important Thing You Need to Know about Taxmageddon…

Plus: How to Legally Shelter Your Portfolio from the Wrath of the IRS Before It's Too Late

By: Dr. David Eifrig Jr., MD, MBA

If you've done the right thing, chances are good you're worried about January 1, 2013.

When I refer to doing "the right thing," I mean you've spent many years earning money for you and your family. You've saved a lot of that money and invested it for the future. And if you really did the right thing, you put a portion of your savings in safe, dividend-paying stocks.

Owning safe, dividend-paying stocks is one of the foundations of a wealthy, worry-free retirement. It's the surest way to grow long-term wealth in the stock market.

But as many retirees know, the morons in Washington D.C. are gearing up to go after your dividend streams, starting January 1.

After all, if you have money to invest, you're one of the nasty "rich people" who needs to pay your "fair share" of taxes. It's your wealth they want to "spread around."

(As for the "change" these taxes are supposed to bring, I'm not seeing it. All I see are more people frisking me in TSA lines... more people on food stamps... and more ridiculous defense spending.)

If you have done the right thing... and you own a stable portfolio of dividend-paying stocks... you've probably heard warnings that any potential new tax will cause a massive selloff in your stocks.

In this special report I've put together for The Project to Restore America, we'll examine this worry. We're going to look at an 85-year history of dividends and taxes in America. As you'll see, what people are worried about isn't a worry at all. And we'll also cover a dividend-paying stock you should own immediately...

Let 'Em Tax Me...

Dividend-paying stocks can have an amazing effect on a diversified, well-balanced portfolio. When executed correctly, reinvesting your dividends over the long term –

through bull markets and bear markets alike – can account for 40% or more of your total gain on stock investments. That's why we want to own businesses that have lasting competitive advantages and treat shareholders well. We can count on these kinds of companies to pay us dividends regularly and consistently over the long run...

But today, many tax-paying Americans are concerned that dividend-paying stocks may suffer if scheduled taxes take effect in January. Right now, laws that cut taxes on dividends to 15% are due to expire at year-end. Unless Congress acts to extend the 2003 tax cut (one of several commonly referred to as the "Bush-era tax cuts"), dividends will once again be taxed at the personal income tax rates.

Some investment advisors are recommending people dump dividend-paying stocks in advance of the change and move toward investments that they say would offer more tax relief. But I disagree...

I've looked at the facts... and we have no reason to worry... The data don't show us a compelling reason to leave behind dividend-paying stocks.

The government has fiddled around with dividend taxes seven times in our history. If you look at changes in the S&P 500 (or the equivalent in years before the benchmark stock index was created), you'll see good news...

In the 20 years leading up to 1936... the government did not tax earnings paid in the form of dividends... It was tax-free income. But in 1936... President Franklin Delano Roosevelt made them fully taxable. (The tax was rescinded four years later.)

As you can see in the table below... stocks rose in the year of the tax hike... and each of the next two years.

Year of Change	**Dividend Tax Rate for Top Tax Bracket...**	**Percentage Change in S&P 500 from One Year Prior To Tax Change Through...**		
	Tax Exempt	**First Of The Year The Tax Law Changes**	**1 Year After The Law Changes**	**2 Years After The Law Changes**
1936	Fully Taxable	41.37%	80.84%	11.05%
1940	Tax Exempt	-5.18%	-19.48%	-33.87%
1954	First $50 Exempt	-6.62%	35.42%	71.17%
1964	First $100 Exempt	18.89%	34.31%	46.48%
1981	First $200 Exempt	25.77%	13.54%	30.29%
1985	Fully Taxable	1.40%	28.10%	46.83%
2003	15%	-23.37%	-3.15%	5.56%
	Average Change	**7.47%**	**24.22%**	**25.36%**

Interestingly – as part of a stimulus plan – the government made dividends tax-exempt again in 1940. And surprise, the stocks fell during the following three years. (Of course, we were fighting World War II at the time.)

In the year before (1939)... the market suffered a big downtrend, which carried

through 1940 and 1941. In 1942, the S&P 500 started back up. But again... there is no strong connection between this uptick and dividends being tax-exempt.

If you look at the following periods – when the government tinkered with how much divided income should be taxed – you see positive gains. The exception is with the 2003 change... when the tax was cut.

Here at The Project... we're not interested in myths and "conventional wisdom." We demand facts and scour them to find the best possible ways for you to invest your hard-earned money. The reality is, changes in dividend taxes don't seem to hurt stock performance... if anything, on average, stocks rise after changes (up or down) in the tax regime.

So you can stop worrying about the dividend-paying stocks in your portfolio – history says they're still great investments.

We have no reason to make any drastic changes to our investments based on the fear of higher dividend taxes. And as always, avoid the emotions of the crowds... They create bad habits for investing.

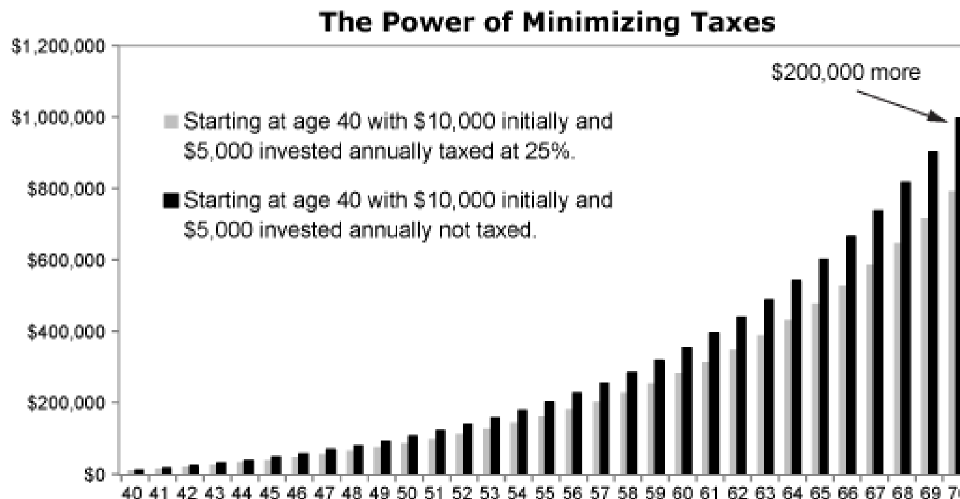
But if you are concerned about taxes eating up much of your dividend payments, there is something you can do to minimize their impact on your investment income.

How to Keep the Government's Grubby Hands Off Your Dividends... for Good

One of the joys of investing is watching your money grow...

Putting your money in investments that continuously build your nest egg means all the difference between having a comfortable retirement and just scraping by.

But the real secret is to do this strategy in a tax-sheltered investment account – also known as an Individual Retirement Arrangement (IRA). Getting money into an IRA allows compounding of returns, without the government shaving off any of the principal. The difference between compounding without paying taxes and paying taxes along the way can be seen in the chart below:



Over 30 years, the tax-deferred account would be worth $996,964.10, while the taxed account would be worth $791,346.60. That's more than $200,000 extra just by avoiding taxes.

Today, several forms and types of IRAs exist...

The two main types of IRAs are traditional IRA and "Roth" IRA (named after Sen. William Roth of Delaware, who sponsored the legislation that created these savings vehicles). When you put money in a traditional IRA, you get a tax deduction for the initial deposit and the government defers taxes on the money until you withdraw the money. As a general rule, you may start taking money out at age 59.5... But you must start taking money out at age 70.5.

With Roth IRAs, you pay taxes on the money before you put it in. Then, when you take out your money in retirement, you don't pay taxes on any of it. This could be especially advantageous for investors who want to shelter their dividend income from higher taxes in the years ahead.

Plus Roth IRAs don't have a required minimum distribution... So you can start withdrawing money when you're 80... 90... or even leave it all for your heirs.

Many people first open their IRA account using a savings account or a certificate of deposit (CD). But today, with savings accounts and CDs yielding less than 1%... you're not getting much for your money by doing that. Other people have IRAs through a brokerage account. This allows you to invest in stocks, bonds, and options... and is what I recommend.

Unchain Your IRA

The best way to manage your IRA is through a self-directed IRA... A typical IRA is managed by the brokerage you hire and limits you to conventional investment choices.

A self-directed IRA is exactly what it sounds like... It puts you in charge of what you invest in. In addition to the conventional investments you can make in a typical IRA – things like stocks, bonds, and options – a fully self-directed IRA allows you to invest in many other things, like real estate (as long as it's not personally used), private stocks, businesses, and even precious metals.

You can invest in just about anything, as long as it's not employed for your personal benefit. For example, you can buy the house next door within your IRA and then rent it to a neighbor. You can also invest in a local small business.

I use my self-directed IRA to generate income by selling stock options. When I use this account for options trading, I have no accounting or tax requirements to follow. I don't have to spend much time during tax season figuring out short- and long-term gains on my option buys and sells.

If you do all your trading inside a retirement account, you won't have to report any trades to the IRS. The goal is just to maximize your total returns as quickly and as easily as you can.

Two investments not allowed within self-directed IRA are collectibles – like cars,

wines, and stamps – and life-insurance contracts.

To open a self-directed IRA, you need to find a custodian that allows you to make your own investments – usually a brokerage or bank. You can call your current brokerage to see if it offers self-directed IRAs. If not, several companies do.

Here are the names of two places you might consider (I get no consideration from any of them) for doing a self-directed IRA:

- PENSCO Trust Company (866-818-4472; www.pensco.com)
- Equity Trust Company (888-382-4727; www.trustetc.com)

Always do your research before investing with any custodian. And be sure you're doing it because you have specific investments in mind.

By following the two strategies we've laid out in this special report – you'll well prepared for the coming fiscal cliff – and able to shield much of your wealth from Taxmageddon – before it's too late.

Here's to our health, wealth, and a great retirement,

Dr. David Eifrig Jr., MD, MBA

Important Note

What you've just read is an excerpt from Dr. David Eifrig's monthly newsletter, Retirement Millionaire.

This report is just one of many he's written over the years... If you've enjoyed it and would like to learn more about Doc and his financial research, click here.