

Rule of 72

This is a formula used to determine the number of years it will take for a debt or investment to double in value: 72 divided by the interest rate equals the number of years to double the value.

$$72 \div \text{rate of return} = \text{years to DOUBLE your money}$$

Example: \$100,000 premium starting at age 35 at 5 % annual interest rate, 28% tax bracket

Taxable	Tax-deferred
\$100,000 premium at 28% tax rate	\$100,000 premium at 0% tax rate
28% tax on 5% = 3.6% net return	0% tax on 5% = 5% net return
$72 \div 3.6\% = 20$ years to double	$72 \div 5\% = 14$ years to double

Account value	At age	Annuity value	At age
\$100,000	35	\$100,000	35
\$200,000	55	\$200,000	49
\$400,000	75	\$400,000	63
		\$800,000	77

When you are ready to take a payout, at least two different options may be available:

1.) Take interest income: (*The interest is considered taxable gain and will be taxed according to your tax bracket.*)

Interest income from \$400,000		Interest income from \$800,000	
\$20,000	Annual interest payment	\$40,000	Annual interest payment
\$20,000	Taxable gain	\$40,000	Taxable gain
(\$5,600)	Taxes at 28%	(\$11,200)	Taxes at 28%
= \$14,000	After-tax annual income	= \$28,800	After-tax annual income

2.) Take a lump-sum payout:

$$\begin{array}{ll} \$400,000 \text{ (tax already paid)} & \$800,000 \text{ less } \$100,000 \text{ cost basis} \\ \$400,000 & = \$700,000 \text{ gain} \\ & \$555,000 \text{ after tax (35% tax bracket)} \end{array}$$

Hypothetical example assumes a constant 5% rate of return, which is not guaranteed and is not intended to represent the actual projected future interest rate.

The Power of Tax – Deferral

This table lists a series of rates for tax-deferred alternatives alongside the rates needed for a bank CD (or other taxable savings product) to generate equivalent net earnings. Unless a CD is an IRA, the CD interest is taxable even if it is left on deposit with the bank.

Table of Equivalent after Tax Yields

Equivalent for Tax-Deferred Alternative	Equivalent CD Rate 28% Tax Bracket
3.00%	4.17%
3.25%	4.51%
3.50%	4.86%
3.75%	5.21%
4.00%	5.56%
4.25%	5.90%
4.50%	6.25%
5.00%	6.94%
5.50%	7.64%
6.00%	8.33%