



# Randhir S. Judge F.L.I.A., LUTCF

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Dear Friends,  
Around this time of the year, we are all aware of how much we pay Uncle Sam in income taxes, and the sales tax that we pay when we shop or enjoy a nice dinner. Although we are not thrilled about it, at least we know that we are paying those taxes. However, many of us have no idea of the "hidden taxes" that we pay. Our article will enlighten you on these taxes that end up taking a big bite out of our wallets.  
With longer life expectancies than men, women tend to live more years in retirement and have a higher chance of exhausting other sources of income. Therefore, it is the women that benefit most from Social Security's cost-of-living protections as benefits are annually adjusted for inflation.  
Please contact me if you have any questions.  
Sincerely,  
Randhir S. Judge

## May 2012

Hidden Taxes: What Is Your True Cost?  
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## Hidden Taxes: What Is Your True Cost?



We are pretty well aware of the taxes we must pay as U.S. citizens; income taxes, payroll taxes, sales taxes, property taxes, and gift and estate taxes, to name a few. We can easily see these taxes on our pay stubs, tax bills, and sales receipts. But there are other taxes imposed on us that you may not be aware of. They are "hidden taxes." And when you add them together with visible taxes, you may be surprised about how high your taxes really are. Here's the rundown on hidden taxes.

### How taxes are hidden

Taxes are hidden in many ways. For example, you see the payroll taxes that are deducted from your payroll check each pay period. What you do not see are the taxes that your employer pays. For example, in addition to income tax, your employer pays half of the Social Security tax as well as unemployment tax on your wages. Like all costs paid by your employer, these taxes get passed on to you as an employee (as a factor in compensation paid), as well as to shareholders and to clients and customers. And if you're receiving dividends from a corporation, keep in mind that taxes have already been paid on that income.

But most hidden taxes are paid by consumers. Sometimes these taxes are disguised as fees, surcharges, tariffs, duties, assessments, dues, excises, levies, licenses, and tolls, among others. And sometimes they're simply rolled into the price of goods and services and are either completely undisclosed or they appear somewhere in the fine print, which is often left unread by the consumer.

### Planes, trains, and automobiles

Many hidden taxes are associated with travel. For example, when you pull up to the pump, you can clearly see the price for the gas, but the "taxes included" disclosure is usually posted somewhere else. How much of what you pay goes to tax revenue? Well, it varies by each state and its tax policy at the time, but it can range from 8¢ per gallon (Alaska) to 47.7¢ per

gallon (California). (Source: Tax Foundation, Tax Data, February 25, 2011)

Taxes associated with traveling by air can include ticket excise tax, flight segment tax, arrival and departure fees, September 11 security fees, passenger facility fees, and--if your travel is international--agricultural inspection, customs, and immigration user fees. There are 16 or more fees that can add up to \$61 (or 20% of your total cost) or more. (Source: Airlines for America, www.airlines.org, 2012) And those are just the U.S. taxes; there can be foreign taxes as well.

Car rental, hotel, and meal taxes can also add up. The GBTA Foundation, the education and research foundation of the Global Business Travel Association (GBTA), reported from its 2011 annual study of the top 50 U.S. travel destination cities that the travel taxes and fees imposed on travel-related services increased the traveler's cost an average of 56% over and above any general sales taxes paid, and that taxes for a single night at the national average room rate of \$95.61 were \$13.12. The combined lodging taxes levied by state, county, and city averaged 13.73%. (Source: News Release, July 21, 2011, www.gbta.org).

### Sin taxes

A seemingly favorite way for government to tax is with the so-called "sin" taxes. Ostensibly, these taxes are imposed to reduce behavior that society considers unhealthy, immoral, or just undesirable in some way. That is why there is a tax on soda, alcohol, tobacco, gambling, and ammunition and firearms. According to the Alcohol and Tobacco Tax and Trade Bureau, revenue collected in 2011 for just some of the above-referenced items totaled approximately \$26 billion. (Source: Statistical Release, December 1, 2011, www.TTB.gov)

### Why are taxes hidden?

Not surprisingly, hidden taxes largely go unnoticed. The result may be that this can make it difficult for us to choose wisely the goods and services that we purchase, or to have a true accounting of our total tax burdens.

# Why Women Need Social Security



*If you have any questions about the Social Security program or the benefits you may be entitled to, visit [www.socialsecurity.gov](http://www.socialsecurity.gov), or call (800) 772-1213.*

Did you know that the first person ever to receive ongoing Social Security benefits was a woman? Ever since Ida May Fuller received the first retirement benefit check in 1940, women have been counting on Social Security to provide much-needed retirement income. Social Security provides other important benefits too, including disability and survivor's benefits, that can help women of all ages and their family members.

## **Retirement benefits: a steady stream of lifetime income**

While Social Security retirement benefits are important for everyone, they are especially important for women. Because women generally live longer and tend to have lower lifetime earnings than men, they may be more dependent on Social Security benefits in retirement.\*

Fortunately, you can count on two features of Social Security to help you provide for a long retirement. First, benefits last as long as you live; although you may exhaust other sources of retirement income, it's impossible to outlive your Social Security retirement income. Second, Social Security benefits are subject to automatic cost-of-living adjustments that increase benefits when prices increase, an especially valuable feature when you have to rely on a fixed income for many years.

When you work and pay Social Security taxes, you earn credits that enable you to qualify for Social Security benefits. You can earn up to 4 credits per year, depending on the amount of income that you earn, and you'll generally need 40 credits (10 years of work) to be insured for retirement benefits. Your monthly retirement benefit will be based on your lifetime earnings. However, if you don't work outside the home or haven't worked long enough to qualify for Social Security based on your own record (or have much lower earnings than your spouse), you may still be eligible based on your spouse's record.

## **Disability benefits: help when you're ill or injured**

During your working years, you may suffer a serious illness or injury that prevents you from earning a living, potentially putting yourself and your family at financial risk. But if you're insured under Social Security, you may be able to get disability benefits if you have worked long enough in recent years, your disability is expected to last at least a year or result in death, and you meet other requirements.

More women than ever are now insured for Social Security disability benefits. According to

the Social Security Administration (SSA), in 1970, only 41% of women were insured; today, approximately 74% of women are insured.\*\* In general, to be insured for disability benefits, you must have earned at least 20 work credits during the last 40 calendar quarters (10 years). If you qualify for benefits, certain family members (such as your dependent children) may also be able to collect benefits based on your work record.

Because eligibility requirements are strict, Social Security is not a substitute for other types of disability insurance, but it can provide basic income protection for working women and their family members.

## **Survivor's benefits: financial protection for your family**

You probably know the value of having life insurance to protect your family, but did you know that Social Security offers valuable income protection as well? If you are insured under Social Security at your death, your surviving spouse (or ex-spouse), your children, or dependent parents may be eligible for benefits based on your earnings record.

You also have survivor protection if you're married and your insured spouse dies. If you're caring for a child who is younger than age 16 or disabled and who is entitled to benefits, you may be entitled to widow's benefits. You may also be entitled to benefits if you are age 60 or older (age 50 or older if you're disabled).

## **Three tips**

- Use the benefit calculators available on the Social Security website to estimate your future retirement, disability, and survivor's benefits. Social Security was never intended to cover all of your financial needs, but understanding what benefits you might be entitled to can help you plan for the future.
- Consider the impact on your Social Security benefits if you plan on taking time out of the workforce. Having years of no or low earnings may mean lower benefits, and can also affect your eligibility for disability coverage.
- Check your earnings history regularly, and report any name changes right away to the SSA so that your earnings are recorded properly. If your name doesn't match SSA records, any income tax refund can also be delayed.

**Sources:** \**Fact Sheet: Social Security Is Important to Women*, SSA Press Office; \*\**Fast Facts & Figures About Social Security, 2011*, SSA

## Pay Down Debt or Save and Invest?



*Should you pay off debt or should you save and invest? To find out, compare what rate of return you can earn on your investments versus the interest rate on the debt. There may be other factors that you should consider as well.*

There are certainly a variety of strategies for paying off debt, many of which can reduce how long it will take to pay off the debt and the total interest paid. But should you pay off the debt? Or should you save and invest? To find out, compare what rate of return you can earn on your investments versus the interest rate on the debt. There may be other factors that you should consider as well.

### Rate of return on investments versus interest rate on debt

Probably the most common factor used to decide whether to pay off debt or to make investments is to consider whether you could earn a higher after-tax rate of return on the investments than the after-tax interest rate on the debt if you were to invest your money instead of using it to pay off the debt.

For example, say you have a credit card with a \$10,000 balance on which you pay nondeductible interest of 18%. You would generally need to earn an after-tax rate of return greater than 18% to consider making an investment rather than paying off the debt. So, if you have \$10,000 available to invest or pay off debt and the outlook for earning an after-tax rate of return greater than 18% isn't good, it may be better to pay off the debt than to make an investment.

On the other hand, say you have a mortgage with a \$10,000 balance on which you pay deductible interest of 6%. If your income tax rate is 28%, your after-tax cost for the mortgage is only 4.32% ( $6\% \times (1 - 28\%)$ ). You would generally need to earn an after-tax rate of return greater than 4.32% to consider making an investment rather than paying off the debt. So, if you have \$10,000 available to invest or pay off debt and the outlook for earning an after-tax rate of return greater than 4.32% is good, it may be better to invest the \$10,000 rather than using it to pay off the debt.

Of course, it isn't an all-or-nothing choice. It may be useful to apply a strategy of paying off debts with high interest rates first, and then investing when you have a good opportunity to make investments that may earn a higher after-tax rate of return than the after-tax interest rate on the debts remaining.

Say, for example, you have a credit card with a \$10,000 balance on which you pay 18% nondeductible interest. You also have a mortgage with a \$10,000 balance on which you

pay deductible interest of 6%, and your tax rate is 28%. So, if you have \$20,000 available to invest or pay off debt, it may make sense to pay off the credit card with \$10,000 and invest the remaining \$10,000.

When investing, keep in mind that, in general, the higher the rate of return, the greater the risk, which can include the loss of principal. If you make investments rather than pay off debt and your investments incur losses, you may still have debts to pay, but will you have the money needed to pay them?

### Some other considerations

When deciding whether to pay down debt or to save and invest, you might also consider the following.

- What are the terms of your debt? Are there any penalties for prepayment?
- Do you actually have money that you could invest? Most debts have minimum payments that must be paid each month. Failure to make the minimum payment can result in penalties, increased interest rates, and default. Are your funds needed to make those payments?
- How much debt do you have? Is it a problem? How do you feel about debt? Is it something you can easily live with or does it make you uncomfortable?
- If you say you will save the money, will you really invest it or will you spend it? If you pay off the debt, you will have assured instant savings by eliminating the need to come up with the money needed to pay the interest on the debt.
- Would you be able to borrow an additional amount, if needed, and at what interest rate, if you paid off current debt? Do you have an emergency fund, or other source of funds, that could be used if you lose your job or have a medical emergency, or would you have to borrow?
- If your employer matches your contributions in a 401(k) plan, you should generally invest in the 401(k) to get the matching contribution. For example, if your employer matches 50% of your contributions up to 6% in a 401(k) plan, getting the 50% match is like getting an instant 50% return on your contribution. In addition, there are tax advantages to investing in a 401(k) plan.

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## What is personal liability insurance and do I have it?

Personal liability insurance protects your assets if you injure another person or damage someone else's property. It's also known as

third-party insurance because it protects you if a third party files a claim against you. Personal liability insurance can be purchased as part of a package policy (such as a homeowners or automobile insurance policy) or as a separate policy (such as a personal umbrella liability policy).

Today, lawsuits are everywhere. What if your dog bites a neighbor? What would happen if someone slips and falls on your front walk?

While you may not be able to avoid all accidents, you can transfer some of the financial risk of the resulting loss to an insurance company by buying personal liability insurance.

How much liability coverage do you need?

Probably more than you think you do. Because there's no optimum amount that applies to everyone, how much personal liability coverage you need depends partly on your tolerance for risk. Can you afford to pay the cost of a claim out of pocket or would even a small claim

threaten your finances? If you already have liability coverage, take a look at your current policy. Determine whether your liability limits are high enough, or if there are any coverage gaps you'd like to fill.

If you own a homeowners or automobile insurance policy or another type of property insurance (e.g., mobile home insurance or renters insurance), you have basic personal liability coverage. These policies will protect you against many liability claims. Your insurance company will defend or settle claims and lawsuits brought against you and pay the sum owed for covered damages (bodily injury or property damage), up to the liability limits of the policy. If you want greater liability coverage limits or if you want broader coverage that includes more types of claims, consider buying a personal umbrella liability policy.

No personal liability insurance policy will protect you against every loss you might face.

Generally, personal liability policies don't cover claims stemming from your business or profession, claims resulting from an act intended to cause injury or damage, and damage to property owned by you.



## What is umbrella insurance and why do I need it?

Umbrella liability insurance (ULI) provides additional liability coverage in excess of the liability coverage provided by other insurance policies,

such as homeowners, renters, and auto insurance. By providing liability protection above and beyond these basic coverages, ULI can protect you against the catastrophic losses that can occur if you are sued. Although ULI can be purchased as a separate policy, your insurer will require that you have basic liability coverage (i.e., homeowners/renters insurance, auto insurance, or both) before you can purchase an umbrella liability policy.

A typical umbrella liability policy provides protection, up to the coverage limits specified in the policy, for vehicle-related liabilities above your basic auto policy; for claims of bodily injuries or property damage caused by you or members of your household; for incidents that occur on or off your property; for non-business-related personal injury claims, such as slander, libel, wrongful eviction, and false arrest; and for legal defense costs for a covered loss, including lawyers' fees and associated court costs.

Policy exclusions vary from one insurer to another, but typically, basic umbrella liability insurance doesn't cover intentional damage caused by you or a member of your family or household; damages arising out of business or professional pursuits; liability that you accept under the terms of a contract or agreement; liability related to the ownership, maintenance, and use of aircraft, nontraditional watercraft (e.g., jet skis), and most recreational vehicles; damage to property owned, used, or maintained by you; damage covered under a workers' compensation policy; and liability arising as a result of war or insurrection.

How much liability insurance do you need? A large judgment against you could easily wipe out your assets and put your future earnings in jeopardy. That's why you should also consider factors such as how often you have guests in your home, whether you operate a home-based business, how much you drive, whether you have teenage drivers in your home, and whether your lifestyle gives the impression that you have "deep pockets." Your insurance professional can help you determine how much coverage you need.