Retirement Planning

401(k)/403(b) Retirement Plans

If you've worked for only one company in your lifetime, you're probably familiar with just one type of retirement savings plan. How do you know if your employer offers a "state of the art" retirement plan? What are other companies offering? If you are one of the many people who have recently suffered a job loss, be sure to take a good look at what kind of retirement plan potential employers offer. It may tip the balance toward taking one job over another, especially if you've had to dip into your retirement savings to keep yourself afloat while you find a new job. Company Match One of the best features an employer can offer in a retirement plan is a company match. Typically the company will match the first few percent of your contribution. It can be a dollar-for-dollar match or something less (like 50 cents for every dollar you contribute). Unfortunately, in the past couple of years we've seen more and more companies eliminate their matching contributions. If you do have a match and you're not taking advantage of it, you're leaving free money on the table. At the very least, you should contribute enough to get the full company match.

Good Selection of Investment Choices

The best retirement plans offer just enough investment choices--not too many and not too few. According to the 45th Annual Survey of Profit Sharing and 401(k) Plans, in 2001 the majority of plans offered 10 or more investment options. The most common investment options are actively managed domestic-stock funds, indexed domestic-stock funds, actively managed international-stock funds, and balanced stock/bond funds. According to the 45th Annual Survey of Profit Sharing and 401(k) Plans, 35% of all plan assets are held in company stock. With well-publicized debacles like the Enron scandal having wiped out the retirement savings of many employees, awareness of the risk of concentrated stock positions has risen. But in many cases employees still hold a disproportionate amount of company stock in their retirement portfolios. The best retirement plans offer special education and/or advice programs dealing specifically with this topic.

IRAs

Both Traditional Individual Retirement Accounts (Traditional IRAs) and Roth IRAs allow taxpayers to save for retirement and reap tax benefits along the way. A check with a short application to a brokerage firm, a mutual fund company, or a bank is usually all it takes to set up one of these accounts.

These two types of IRAs offer tax advantages at different times. The rules governing Traditional IRAs allow a taxpayer to deduct his contributions upfront on his tax return in the year he puts money into the account, presumably when he is in a higher tax bracket, but require that he pay income tax when he later withdraws the money upon retirement, presumably at that time he would be in a lower tax bracket. A beneficiary who receives distributions from a decedent's Traditional IRA usually also must pay income tax on the amounts received.

Using a Roth IRA, on the other hand, generates no upfront tax deduction to the taxpayer when he contributes to the account but the withdrawals, either made by herself or her beneficiaries, are usually free from income tax. Roth IRAs are particularly attractive to younger taxpayers whose retirement accounts may appreciate substantially by the time they are ready to make withdrawals.

Every year, taxpayers have until April 15th to contribute to their Traditional and Roth IRAs and have the contribution count toward the previous year. Contributions made at the beginning of the year should be clearly designated either for the current year or the previous year, and contributions made to a Traditional IRA designated for a previous year will reduce the prior year's tax liability.

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Contributing Limits to IRAs

Each year, the IRS changes the rules governing individual retirement accounts, so it is important to stay current on the new regulations for your IRA, especially when opening a Roth IRA. The rules that govern your annual maximum contribution to your individual retirement account depend upon your age: one set of regulations if you are under 50 this year, and another set of rules if you turn 50 or older this year.

If you are under 50 in 2013, the maximum IRA limit for contributions that you can make is five thousand five-hundred dollars, up to the amount you made in taxable income this year. So if you only made four thousand dollars this year, this is the maximum you can contribute. This applies to both traditional and Roth IRA limits. If you turn 50 or older this year the most you can contribute to your individual retirement account is six thousand five-hundred dollars, up to but not exceeding your 2013 taxable income. This amount includes the five thousand dollar limit that everyone qualifies for, as well as an addition one thousand catch-up contribution. Income limits apply!

In 2012 the annual limit for your IRA contribution was five thousand dollars, for those 50 and under. If you were over 50 in 2012, the catch-up contribution rules increased your maximum limit to $6000.

Eligibility

Certain high-income individuals either may not be allowed to deduct contributions made to Traditional IRAs or may find the amount they are allowed to deduct somewhat limited. A taxpayer who participates in his company's qualified pensions plan and has annual income over a specific amount may not deduct contributions to his Traditional IRA. That income amount in 2006 was $85,000 for married taxpayers filing joint returns, and $60,000 for single taxpayers. Furthermore, a taxpayer who makes $160,000 or more a year may not deduct contributions to a Traditional IRA if their spouse participates in a company retirement plan.

In addition, there are limits on a taxpayer's ability to contribute to Roth IRAs. For example, married taxpayers filing joint returns with annual income of at least $160,000 and single taxpayers with at least $110,000 in annual income are not allowed to contribute to a Roth IRA. On the other hand, unlike Traditional IRAs, a taxpayer's participation in a pension plan has no effect on her ability to contribute to a Roth IRA.

Accessibility

Because IRAs are meant for retirement, a taxpayer who withdraws funds from either her Traditional IRA or Roth IRA before she turns 59½ will incur a 10% penalty tax assessed on the withdrawn amount. Note that this is in addition to any income tax owed on the amount withdrawn. The IRS usually forgives the penalty when the money is withdrawn for one of a limited number of purposes that include, for example, the taxpayer's disability, or the purchase of a first home. After a taxpayer turns 70½ he must start withdrawing from his Traditional IRA. This is because the Traditional IRA is a retirement planning vehicle and not a means to indefinitely accumulate assets income-tax free. With respect to Roth IRAs, there is no requirement that taxpayers withdraw funds since withdrawals would not be subject to income tax anyway.

Care should be taken when IRAs are to be inherited by a child or spouse because, with proper planning, payments may be deferred thereby postponing the income tax burden to the recipient. Finally, although IRAs can be used for sheltering income tax while the taxpayer is alive, at the taxpayer's death they trigger estate tax considerations that should be addressed.

Sources: http://www.prattlaw.com/ http://iracontributionlimits2010.com/