

Retirement Planning with IRAs

Maybe you participate in an employer's retirement savings plan. Maybe not. Either way, an individual retirement account (IRA) can play an important role in your retirement planning.

An IRA offers you a flexible and tax-advantaged opportunity to invest for your future financial needs. During your working years, you may contribute every year, but you aren't *required* to do so. In addition to your annual contributions, an IRA can receive rollover contributions from other retirement plans, allowing you to streamline the management of your retirement assets.

There are two basic types of IRAs: traditional and Roth. Each has specific tax advantages and requirements that you'll want to become familiar with before investing.

Lower Your Current Taxes with a Traditional IRA

Your annual contributions to a traditional IRA will be tax deductible if you meet certain tax law requirements. As an added benefit, IRA investment earnings are tax deferred. The combination of these tax advantages allows you to accumulate more in a

deductible IRA than you could by investing on an after-tax basis in a comparable taxable account.

For your IRA contributions to be deductible, you must meet *one* of the following conditions:

- Neither you nor your spouse can be an active participant in an employer-sponsored plan, or
- If you (and/or your spouse) actively participate in an employer's plan, your adjusted gross income (AGI) must be below a certain level

As the table shows, the IRA deduction is phased out for plan participants when AGI falls within specified ranges.

IRA DEDUCTION PHASEOUT RANGES FOR PLAN PARTICIPANTS

Year	2012**
Joint Return*	\$92,000-\$112,000
Single, Head of Household	\$58,000-\$68,000
Married Filing Separately	\$0-\$10,000

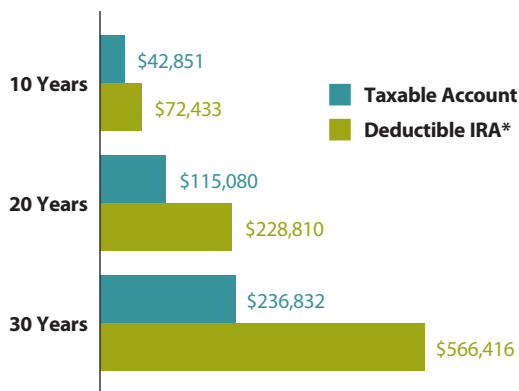
* The phaseout range for a married person who isn't a plan participant but whose spouse is a participant is \$173,000-\$183,000.

** Subject to annual inflation adjustments.

TAX-DEDUCTIBLE IRA VERSUS FULLY TAXABLE INVESTMENT ACCOUNT

Assume:

- Tax bracket is 33% (other tax rates may apply to you).
- Annual IRA contribution is \$5,000 (contribution limit for 2012).
- Annual taxable account contribution is \$3,350 (\$5,000 – 33% tax).
- Average annual investment return is 8% for both accounts (33% tax is subtracted each year from the taxable account's earnings).



* The IRA balance will be taxed on distribution.

This illustration is hypothetical and does not represent any actual investment. Nor does it take into account any fees or charges that might be deducted from the accounts.

Source: NPI

If you wish to, you may contribute to a traditional IRA even if you don't qualify for deductible contributions. With a nondeductible IRA, you still receive the benefit of tax deferral on your investment

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earnings. However, before you make nondeductible contributions to a traditional IRA, you may want to see whether you're eligible to contribute to a Roth IRA.

So far, you've read about the tax treatment of traditional IRA contributions and earnings. What about account withdrawals? They're subject to income taxes at ordinary rates. The exception: Amounts attributable to nondeductible contributions are returned to you tax free.

Enjoy Tax-free Withdrawals with a Roth IRA

Unlike traditional IRA contributions, Roth IRA contributions are always made on an after-tax basis — that is, you may not deduct your contributions to a Roth IRA. As with a traditional IRA, Roth IRA investment earnings are tax deferred. However, withdrawals from a Roth IRA are *tax free* if you meet certain requirements. This means that the earnings are *never* subject to income tax.

To gain this special tax treatment, funds must remain in your Roth IRA for a five-year period. This period begins with the first taxable year for which you make a contribution. After that, earnings may be distributed from your Roth IRA tax free:

- Once you have reached age 59½
- To your beneficiaries after your death
- If you become disabled
- In order to pay qualified first-time homebuying expenses of up to \$10,000 (lifetime limit)

Withdrawals of original Roth IRA *contributions* are not subject to any tax-related restrictions. However, the ability to contribute to a Roth IRA is limited for higher income individuals. For 2012, Roth contributions are phased out for joint filers with AGI between \$173,000 and \$183,000. For most other filers, the phaseout range starts once AGI exceeds \$110,000, with full phaseout at \$125,000. The phaseout range for married-separate filers is \$0 to \$10,000.

IRA Contribution Limits

The annual contribution limit for IRAs in 2012 is \$5,000. This limit is subject to annual inflation adjustments. You may contribute up to

the annual limit or 100% of your compensation, whichever is less. Married couples may contribute twice as much — even if one spouse doesn't earn compensation. Note that the limit caps your annual contributions to *all* of your IRAs, traditional and Roth, not to each individual account. If you are age 50 or older, you also may make additional "catch-up" contributions of up to \$1,000 per year.

Roth IRA contributions are allowed even after you've reached age 70½. So, if you wanted to continue saving *during* your "retirement" years, you could continue contributing to your Roth IRA, assuming you were working and earning compensation.

Receiving Distributions from an IRA

If you withdraw money from a traditional IRA before age 59½, you may be subject to a 10% penalty tax in addition to ordinary income tax. Some early withdrawals are not subject to the penalty, however. These include distributions made due to disability, for certain medical expenses, or for qualified homebuying or higher education costs.

On the other hand, the tax law does not allow you to leave money in a traditional IRA indefinitely. After you reach age 70½, you must take annual required minimum distributions (RMDs). The RMD is calculated using an IRS table. The deadline for the first RMD is April 1 of the year following the year in which you reach age 70½.

With a Roth IRA, however, there are no RMD rules during your lifetime. This makes a Roth IRA an excellent estate planning tool if you want to provide a potential source of tax-free funds to your children or other beneficiaries. While IRA beneficiaries are subject to RMD requirements, they generally may stretch distributions over their life expectancies if desired.

Converting a Traditional IRA into a Roth IRA

You may roll over a traditional IRA into a Roth IRA if you feel a Roth IRA would better suit your planning needs. However, any taxable amounts that are rolled over generally must be included in your income in the tax year in which the rollover occurs.

Traditional or Roth. The choice is yours. Either type of IRA can help you reach your retirement goals.

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