



Investment Insights

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IRA Season Is Upon Us

With the April 15th tax-filing deadline rapidly approaching, many of you are again considering funding individual retirement accounts. Individual retirement accounts come in two forms: regular Individual Retirement Accounts (IRA's), and the newer ROTH IRA's. Both can be great ways to save for retirement, and can also help to supplement company-sponsored retirement accounts you may already participate in such as 401(k) Plans, 403(b) Plans, or Profit Sharing Plans. Your deadline for making contributions to these accounts is April 15th, so the time to act is now. Here is a primer on IRA's and ROTH IRA's.

IRA's

Any individual with compensation is eligible to contribute to a traditional IRA account. For the tax year 2001, your contribution is limited to the lesser of a maximum of \$2,000 or your compensation for the year. This limit will rise in tax year 2002 to \$3,000 for Californians if the state complies with the new Federal limits. Your contribution to a traditional IRA is tax-deductible if you are not covered by a retirement plan at work (be careful: if you choose not to participate in your company-sponsored retirement plan, you may still be considered "covered" by the plan, and thus cannot deduct your IRA contribution—check with your company on this). If you are covered by a plan at work, you may still be able to deduct your IRA contribution if your Modified Adjusted Gross Income is below \$32,000 filing individually or \$52,000 for a married couple filing jointly.

The benefits of a traditional IRA include (potentially) an immediate tax deduction of your contribution from your taxable income, and tax-deferred growth of your money until you withdraw it at retirement. When you retire, withdrawals are taxed as ordinary income. The drawback is that any withdrawals made before age 59 ½ are subject to taxation and a 10% penalty by the IRS. Tax law changes in 1997 allow for certain penalty-free distributions for first-time home purchases (maximum of \$10,000), death, disability, and other defined events.

ROTH IRA's

ROTH IRA's are almost like the inverse of a traditional IRA—contributions are not tax-deductible, but withdrawals made after age 59 ½ are tax-free. ROTH IRA's are not

available to all taxpayers: the IRS does phase-out eligibility for individuals with more than \$95,000 in Adjusted Gross Income (AGI), or couples with more than \$150,000 in AGI. A nice feature of ROTH IRA's is that you can still be eligible even if you are covered by a company-sponsored retirement plan. Contribution limits are \$2000 for tax year 2001, and, again, if the state of California adopts the new Federal laws, limits will rise to \$3,000 for tax year 2002.

The benefits of a ROTH IRA are similar to an IRA in that you enjoy tax-deferred growth during the life of the account. However, you don't get the immediate write off on your current tax return. This can be more than offset by the fact that your withdrawals will not be taxed once you reach age 59 ½ and begin to take money out of the account. Basically, you can view this as the IRS taking their cut up front, versus IRA's, where they get their cut when you withdraw the money.

If you feel a little confused by all of this, you are not alone. The best thing to do is to discuss your options with your tax preparer and your investment professional and get their input as to which plan may work best for your situation.

Here are three final tips on contributing to an IRA or ROTH IRA. First, you need not set up a new account every year to accommodate your contribution: in fact, you are best off making your annual contribution to your existing account to avoid confusion and added expenses of maintaining multiple accounts.

Second, be sure to consider investing your contributions in a vehicle that suits your investment goals: too often, investors put all of their contributions into fixed-interest accounts like CD's that, over time, may generate low rates of return. In the case of a 30-year old, the difference between annual returns of 4% versus 10% (the 75 year average return of large-company common stocks) on your money, compounded over 20 years, can add up to tens of thousands of additional dollars available to you come retirement.

Thirdly, consider making your 2002 contribution now rather than waiting until April of 2003. This gives your money an additional 12 months to grow for you tax-deferred!

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