

Money Matters

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How to Maximize Your IRA Investments

By Aaron Skloff AIF, CFA, MBA

Q: Even though it is 2012, can we still contribute to Individual Retirement Accounts for 2011?

The Problem – Foregoing Financial Planning and Tax Planning Strategies for 2011

Assuming financial planning and tax planning strategies for 2011 ended on Dec. 31, 2011 is a completely logical assumption. Despite being a logical assumption it is also incorrect. Unfortunately, logical assumptions can sometimes harm your financial health.

The Solution - Utilizing Financial Planning and Tax Planning Strategies for 2011

One of the most powerful estate, financial, retirement and tax planning strategies is the use of the Individual Retirement Account (IRA). Fortunately, you can establish and contribute to an IRA for the tax year 2011 up until the time you file your 2011 taxes (with a deadline of April 17). If you have a Keogh or Simplified Employee Pension (SEP) IRA you can receive a filing extension, extending your contribution deadline to Oct. 15. Although the qualifications and contribution limits are straight forward, the type of IRA or IRAs you may qualify for requires a bit of research.

Qualifying for an IRA

Whether you earn over \$1 million per year or absolutely no income you can still qualify for an IRA. Even a child who earns income delivering newspapers can qualify for an IRA. In order to qualify for an IRA as a non-earner, your spouse must generate earned income (note: alimony is an exception). Earned income includes salary, self-employed income and sales commissions. It does not include interest, dividends, pension income or social security income.

IRA Contribution Limits

Contributions are limited to the lesser of earned income or \$5,000 (same for 2012) for those under the age of 50 or \$6,000 (same for 2012) for those aged 50 and over. For example, a 65-year-old retired husband and 63-year-old semi-retired wife, who earns \$12,000, could each contribute \$6,000 to an IRA in 2011. As another example, a 12-year-old part-time newspaper deliverer, who earns \$3,000, could only contribute \$3,000.

Traditional IRA

Contributions are fully tax-deductible if you are ineligible to participate in an employer-sponsored retirement plan. Otherwise, the deduction begins to phase-out once your Modified Adjusted Gross Income (MAGI) exceeds \$56,000 (\$57,000 for 2012) for single filers or \$90,000 (\$91,000 for 2012) if both persons are covered and married filing jointly. With or without a deduction, earnings in a Traditional IRA are sheltered from taxes until they are withdrawn. Traditional IRAs provide powerful estate planning benefits, since the taxes on all capital gains, dividends and interest are deferred until assets are withdrawn. Withdrawals are generally not required until you reach age 70½, based on Required Minimum Distributions (RMDs) rules.

Roth IRA

Contributions are never deductible and eligibility begins to phase-out once your MAGI exceeds \$107,000 (\$110,000 for 2012) for single filers or \$169,000 (\$173,000 for 2012) for those married filing jointly. The Roth IRA has a very important distinction from the Traditional IRA. Not only is income sheltered from taxation while in the Roth IRA, but withdrawals are tax free. A Traditional IRA is like 'having your cake,' while a Roth IRA is like 'having your cake and eating it too.' Roth IRAs provide powerful estate planning benefits, since the taxes on all capital gains, dividends and interest are tax free when assets are withdrawn. The original owner of a Roth IRA is not subject to RMD rules, further highlighting its estate planning benefits.

Action Step – Start Your IRA

Question not, 'Should I start an IRA?'; question, 'Which IRA should I start?' With such liberal restrictions, most people qualify for an IRA. The government realizes Social Security and Medicare are broken, while the costs in retirement are ballooning. Thus, it has essentially given taxpayers a gift in the form of an IRA. Do not look a gift horse in the mouth – contribute to an IRA before the deadline and gain estate, financial, retirement and tax planning benefits.

Aaron Skloff, Accredited Investment Fiduciary (AIF), Chartered Financial Analyst (CFA), Master of Business Administration (MBA) is CEO of Skloff Financial Group, a Registered Investment Advisory firm based in Berkeley Heights. He can be contacted at www.skloff.com or 908-464-3060.