

IRAs - The Basics

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An I-R-A is an Individual Retirement Account although for many Americans it stands for *Involved* or even *Inexplicable* Retirement Account.

According to a recent survey by a subsidiary of AARP, 44% of adults don't really understand how IRAs work and more than a third aren't sure or don't know whether they're eligible to contribute to one.

So let's take a look at IRA basics.

An IRA is simply a personal account that gives you tax advantages for saving for retirement. There's a wide range of IRA investments. There are certificates of deposit, stocks, bonds, and mutual funds (and even more choices under what's called self-directed IRAs).

There are actually eleven types of IRAs but the two people hear about the most are the traditional IRA and the Roth IRA. Both will allow you to accumulate wealth without paying taxes on your profits along the way. But the basic big difference between the two:

- the traditional IRA offers *tax-deferred* savings meaning the money you deposit isn't taxed until you withdraw that money (hopefully many years later)
- the Roth offers *tax-exempt* savings meaning you **never** pay taxes on your gains as long as you follow the rules).

Translation: the traditional IRA ultimately sticks you with a tax bill for those profits. The Roth doesn't.

With the traditional IRA:

- you may be eligible to deduct your contributions
- if you can't deduct contributions, earnings grow tax-deferred until withdrawn
- withdrawals are taxable
- withdraw *before* age 59 1/2, in most cases you'll have to pay both income tax and a 10% penalty
- people age 50 and older can make an additional \$1000 "catch up" contribution each year (though two-thirds of Americans in the recent survey didn't know this).

With the Roth IRA:

- contributions are never deductible
- available to single filers earning up to \$95,000 annually
- to couples making up to \$150,000
- great flexibility
- withdrawals (including earnings) are **tax free**

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- **if** the IRA has been open for at least 5 tax-years
- and **if** you're older than 59 1/2
- as long as you follow the rules, *you never pay taxes on your gains.*

Many people unfortunately, believe they have until the October 15th tax-filing extension deadline to contribute to their IRA. This is unfortunate and incorrect. If you're going to make an IRA contribution for this year, it must be made no later than April 15th, 2010.

Here's to your health and wealth.

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