Retirement Plan
Update
Issue 1, 2018
Because the time is now...

Keeping up with your IRA

If you're one of the millions of American households who owns either a traditional individual retirement account (IRA) or a Roth IRA, then the onset of tax season should serve as a reminder to review your retirement savings strategies and make any changes that will enhance your prospects for long-term financial security. It's also a good time to start an IRA if you don't already have one. The IRS allows you to contribute to an IRA up to April 18, 2018 for the 2017 tax year.

This checklist will provide you with information to help you make informed decisions and implement a long-term retirement income strategy.

Which account: Roth IRA or traditional IRA?

There are two types of IRAs available: the traditional IRA and the Roth IRA. The primary difference between them is the tax treatment of contributions and distributions (withdrawals). Traditional IRAs may allow a tax deduction based on the amount of a contribution, depending on your income level. Any account earnings compound on a tax-deferred basis, and distributions are taxable at the time of withdrawal at then-current income tax rates. Roth IRAs do not allow a deduction for contributions, but account earnings and qualified withdrawals are tax free.[1]

In choosing between a traditional and a Roth IRA, you should weigh the immediate tax benefits of a tax deduction this year against the benefits of tax-deferred or tax-free distributions in retirement.

If you need the immediate deduction this year — and if you qualify for it — then you may wish to opt for a traditional IRA. If you don't qualify for the deduction, then it's almost certainly a better idea to fund a Roth IRA.

Case in point: Your ability to deduct traditional IRA contributions may be limited not only by income, but by your participation in an employer-sponsored retirement plan. (See callout box below.) If that's the case, a Roth IRA is likely to be the better solution.

On the other hand, if you expect your tax bracket to drop significantly after retirement, you may be better off with a traditional IRA if you qualify for the deduction. You could claim an immediate deduction now and pay taxes at the lower rate later. Nonetheless, if your anticipated holding period is long, a Roth IRA might still make more sense. That's because a prolonged period of tax-free compounded earnings could more than make up for the lack of a deduction.

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Should you convert to Roth?

The IRS allows you to convert — or change the designation of — a traditional IRA to a Roth IRA, regardless of your income level. As part of the conversion, you must pay taxes on any investment growth in — and on the amount of any deductible contributions previously made to — the traditional IRA. The withdrawal from your traditional IRA will not affect your eligibility for a Roth IRA or trigger the 10% additional federal tax normally imposed on early withdrawals.

The decision to convert or not ultimately depends on your timing and tax status. If you are near retirement and find yourself in the top income tax bracket this year, now may not be the time to convert. On the other hand, if your income is unusually low and you still have many years to retirement, you may want to convert.

Maximize contributions

If possible, try to contribute the maximum amount allowed by the IRS: $5,500 per individual, plus an additional $1,000 annually for those age 50 and older for the 2017/2018 tax years. Those limits are per individual, not per IRA.

Of course, not everyone can afford to contribute the maximum to an IRA, especially if they're also contributing to an employer-sponsored retirement plan. If your workplace retirement plan offers an employer's matching contribution, that additional money may be more valuable than the amount of your deduction. As a result, it might make sense to maximize plan contributions first and then try to maximize IRA contributions.

Review distribution strategies

If you're ready to start making withdrawals from an IRA, you'll need to choose the distribution strategy to use: a lump-sum distribution or periodic distributions. If you are at least age 70½ and own a traditional IRA, you may need to take required minimum distributions every year, according to IRS rules.

Don't forget that your distribution strategy may have significant tax-time implications if you own a traditional IRA, because taxes will be due at the time of withdrawal. As a result, taking a lump-sum distribution will result in a much heftier tax bill this year than taking a minimum distribution.

The April filing deadline is never that far away, so don't hesitate to use the remaining time to shore up the IRA strategies you'll rely on to live comfortably in retirement.

Traditional IRA deductible contribution phase-outs

Your ability to deduct contributions to a traditional IRA is affected by whether you are covered by a workplace retirement plan.

If you are covered by a retirement plan at work, your deduction for contributions to a traditional IRA will be reduced (phased out) if your modified adjusted gross income (MAGI) is:

- Between $99,000 and $119,000 for a married couple filing a joint return for the 2017 tax year ($101,000-$121,000 in 2018).
- Between $62,000 and $72,000 for a single individual or head of household for the 2017 tax year ($63,000-$73,000 in 2018).

If you are not covered by a retirement plan at work but your spouse is covered, your 2017 deduction for contributions to a traditional IRA will be reduced if your MAGI is between $186,000 and $196,000 ($189,000-$199,000 in 2018).

If your MAGI is higher than the phase-out ceilings listed above for your filing status, you cannot claim the deduction.

Roth IRA contribution phase-outs

Your ability to contribute to a Roth IRA is affected by your MAGI. Contributions to a Roth IRA will be phased out if your MAGI is:

- Between $186,000 and $196,000 for a married couple filing a joint return for the 2017 tax year ($189,000-$199,000 in 2018).
- Between $118,000 and $133,000 for a single individual or head of household for the 2017 tax year ($120,000-$135,000 in 2018).

If your MAGI is higher than the phase-out ceilings listed above for your filing status, you cannot make a contribution.

Source/disclaimer:

[1] Early withdrawals (before age 59½) from a traditional IRA may be subject to a 10% additional federal tax. Nonqualified withdrawals from a Roth IRA may be subject to ordinary income tax as well as the 10% additional tax.

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20182-CAS (01/18)