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21st century retirement

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Roth IRAs for Kids

It may be difficult to convince your teenagers to participate in their financial futures, but if you can persuade them to contribute at least part of their babysitting or after-school job money to a Roth Individual Retirement Account (IRA), they may thank you later.

Anyone with earned income below $132,000 for single filers and $194,000 for married joint filers in 2016 can open a Roth IRA retirement account. Contributions are nondeductible, but earnings and qualifying distributions accumulate tax free. Because children seldom make enough to owe income tax, they are usually better off with a Roth IRA than a tax-deferred traditional IRA. For 2016, your child can contribute up to $5,500 (or earned income, whichever is less) to a Roth IRA.

Saving for retirement early can generate substantial results. Suppose your 14-year-old daughter uses $1,000 to open a Roth IRA. If she makes no additional contributions and the funds grow at 8% annually, she will have more than $50,000 to withdraw tax free at age 65. Or suppose your son opens a Roth IRA with $2,000 when he is 15-years-old, and then he contributes $2,000 annually for the next 10 years. The estimated value of his tax-free fund balance at age 65 will exceed $700,000, if the annual growth rate is 8%.*

A Roth IRA offers the greatest growth potential if the account is left untouched until the holder reaches the age of 59½. At that age, the holder can withdraw earnings tax free, provided he or she has owned the account for five years. The IRS does permit penalty-free early withdrawals to pay for education or to help with a first-time home purchase. However, taxes will be owed on nonqualified early withdrawals.

Before you open a Roth IRA for your child, keep in mind that you cannot stop your child from withdrawing money from the account whenever he or she wants after reaching the age of majority, which is 18 in most states. If you are uncertain about your child's ability to handle money, opening an account in his or her name may not be the best choice.

Also, be aware that only taxable compensation income can be contributed to a Roth IRA. In general, paying your children for doing chores around the house does not qualify as compensation income, as this is an intrafamily transaction not usually reported to the IRS. However, if you own your own business, you are permitted to hire your minor children to do certain jobs.

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Putting the Pieces of Your Retirement Puzzle Together

If life is a journey, retirement is the destination where you reap the hard-earned rewards for decades of working. But, as with most good things in life, a comfortable retirement doesn't just happen without effort. It requires a sound, comprehensive financial strategy.

Retirement planning can be like a jigsaw puzzle. Once you put the interlocking pieces together, you will be ready to develop a retirement plan that will meet your financial goals. Let's look at the following four pieces of the puzzle:

1. **Social Security—**Most working Americans will receive Social Security benefits that provide a basic level of retirement income based on the length of time worked, amount of earned income, and age at retirement.
2. **Employer-sponsored pension plans—**If you have a defined benefit or pension plan, your employer provides a retirement benefit in the form of either monthly income or a lump sum. The amount of your benefit is generally based on your salary, length of service, and a benefit formula that averages the employee's earnings over a prescribed period of time.
3. **Employer-sponsored retirement plans—**If your employer sponsors a defined contribution plan, such as a 401(k), you may contribute a percentage of your pre-tax income to a retirement account, as defined by the company plan. Your employer may also match a percentage of your contributions. Earnings have the potential to grow tax-deferred.
4. **Personal savings—**Personal retirement savings may be key to achieving your financial goals. A disciplined savings program can help you accumulate additional assets to supplement Social Security benefits and employer-sponsored plan funds.

Taking Action

Your first step is to assemble the pieces of your retirement planning puzzle to determine if your projected income and assets will be sufficient to fund a comfortable retirement. Although Social Security and any employer-sponsored pension plan offer relatively fixed benefits, you may be able to increase your 401(k) contributions and personal savings to supplement any expected shortfall. Regular contributions and tax-efficient vehicles can help build your assets over time.

If possible, maximize contributions to your 401(k) or other employer-sponsored retirement plan. Contributions to a 401(k) come from pre-tax salary, and taxes on both contributions and earnings are deferred until you retire. Note that there are limits to the amount you can contribute each year.

You may also choose to contribute to an Individual Retirement Account (IRA). If you are under age 50, up to $5,500 may be contributed to an IRA or a combination of IRAs in 2016. For those age 50 and over, an additional $1,000 may be contributed. Contributions to a traditional IRA may qualify for a tax deduction, and earnings have the potential to grow tax deferred. However, taxes will be owed on withdrawals in retirement, without penalty, if you are over age 59½. Contributions to a Roth IRA are not tax deductible, but earnings have the potential to grow tax free. Distributions in retirement are also tax free, provided you have owned the account for five years and are at least age 59½.

Whether you are in your 30s, 40s, or 50s, *now* is the time to start planning for your retirement. Be sure to consult a qualified financial professional to help you devise a strategy for the retirement you envision. ■

Updating Your Will Can Contribute to a Relaxing Retirement

Whether you are decades or months away from retirement, it may be prudent to review your will whenever there is a significant change in your family circumstances or finances. To stay current, revisit your will at least once every five years to help ensure your estate tax strategies are on track, and that your assets will be distributed according to your wishes.

Seek Counsel

Legally, you could draft a will on your own. However, it is recommended that a will be drawn up by a lawyer. The reasons include the inherent complexity of estate planning and that states have different standards and often require specific language for a will to be deemed valid. If you draft your own, have your will *reviewed* by a lawyer so you can be assured that all statutory requirements are met.

A married couple may draft a will jointly or separately as individuals. Separate wills may help specify *who* owns *what* property. The portion of your estate covered by a will includes *tangible* assets, such as your home or car, as well as *intangible* assets, such as savings accounts held in your name. (Property owned jointly with right of survivorship will pass directly to the surviving owner, while other assets, such as life insurance death benefits, will automatically pass to your designated beneficiaries.)

Be Thorough

Whenever you update your will, the new document should include the date, a statement revoking all previous wills, provisions for trusts (if any), names of guardians and alternates for minor children (if necessary), and specific bequests. A specific bequest calls for the transfer of *a particular piece* of property to a named beneficiary, while a general bequest does not specify from which part of an estate the property is to be taken. Be sure that the updated and signed document also includes your full name, a statement that the document is a will, and the names of the executor and substitute executor.

Once you have reviewed and updated your will, make copies for yourself and family members, or others who may need the information. Be sure the original is kept in a secure place, such as a bank safe-deposit box or lawyer's office. Also, make sure your family and friends know where the will is located. Once these tasks are completed, you can feel confident, knowing that your wishes will ultimately be fulfilled. ■

roth iras for kids

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Provided you pay your children a fair market wage for the services performed, their earnings would be considered compensation income and could be invested in a Roth IRA.

It is essential to keep detailed records of how the money placed in a Roth IRA was earned, even if a teenager's working arrangements were informal (e.g., babysitting or mowing the lawn for neighbors) and he or she did not earn enough to owe income tax. Penalties could apply if the IRS determines the funds contributed to a Roth IRA were not compensation income.

The good news is that if, for example, your teenage son goes out and blows his paycheck on a new smartphone and skateboard, all is not lost. If he earned $2,500 over the summer but spent all the money, you could still contribute the amount equivalent to his taxable earnings into a Roth IRA on his behalf, thereby helping to ensure that at least some funds have been set aside for his retirement, when skateboarding days are behind him. ■

** These hypothetical examples are for illustrative purposes only. They are not intended to reflect an actual security's performance. Investments involve risk and may result in a profit or a loss. Seeking higher rates of return involves higher risks.*

Raising the Retirement Age for Less-Educated Workers May Be Unfair

Although policymakers have been calling for an increase in the statutory retirement age to reflect rising longevity, the recent widening of life expectancy disparities based on socioeconomic status (SES) could mean that raising the age of retirement would be unfair to less-educated workers, according to a study published by the Center for Retirement Research at Boston College.

The research brief, "Does a Uniform Retirement Age Make Sense?" by Geoffrey T. Sanzenbacher, Anthony Webb, Natalia S. Orlova, and Candace M. Cosgrove, was published in January 2016. The authors observed that, in the face of rising life expectancies, many policy experts argue that today's workers can retire later and still spend the same fraction of their lives in retirement as past generations. The researchers pointed out, however, that while such an argument assumes that workers across the socioeconomic spectrum have experienced similar increases in life expectancy, the evidence suggests that life expectancies for low-SES individuals have been improving more slowly than for high-SES individuals in recent decades.

The analysis used data from the National Longitudinal Mortality Study (NLMS) to estimate trends in mortality from 1979-2011 by education among individuals aged

25 or older. Education, which is a common measure of SES, was defined by quartiles of educational attainment. The authors then used these estimates to determine how much longer each educational group could work today if the goal is to maintain the same ratio of retirement years to working years as the ratio that existed in 1979.

The results showed that the period life expectancies for each gender and educational quartile reflected recent mortality improvements: conditional on surviving until age 65.8, life expectancy increased from 1979 to 2011 by 4.0 years for the least educated men and 6.1 years for the most educated men, and by 1.4 years for the least educated women and 3.2 years for the most educated women.

Based on these life expectancy figures, the analysis then looked at the ratio of the years spent in retirement to the years spent working, calculating the age to which individuals in each cohort could work in 2011 to achieve the same ratio as in 1979. The results showed that while all of the SES groups could work longer while maintaining their 1979 ratio of retirement to work years, because mortality inequality had increased considerably, those in the lowest quartiles could not work as long. The men in the lowest quartile could work until age 68.1 while the men in the highest quartile could work until age 69.6, a gap of 1.5 years. Similarly, the women in the lowest quartile could work until age 66.0 while the women in the highest quartile could work until age 67.2, a gap of 1.2 years.

While acknowledging that today's workers can, regardless of their SES, work longer while still spending similar proportions of time working and in retirement as their counterparts who retired 30 years earlier, the authors emphasized that policies that seek to extend work life while treating all workers the same will tend to cut into the retirement of low-SES workers more than that of high-SES workers. They therefore recommended that policymakers seeking to encourage working longer should be cautious about the potential effects that such policies could have on inequality. ■

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