Your Guide To Popular Retirement Plans

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Introduction

Most American workers are offered some sort of retirement plan by their employer—whether it's an IRA, profit sharing, or some other flavor of savings account.

About 135 million (1) of us currently participate in a workplace retirement plan, which accounts for about 54 percent of the national workforce.

Many of these plans are excellent investment vehicles to save for retirement. But how does one go about picking the right plan? Depending on what sector of the economy you work in, you may only have access to a limited selection of the various types of plans offered today.

Since many of them have complicated rules and regulations, we will define each type of investment vehicle and highlight the pros and cons, advantages and disadvantages, penalties, taxes, limitations, opportunities, and ideal candidates.

By the time you are done reading this e-book, you should have a better understanding of the types of plans offered by your employer, the basic rules that apply to investing in them, and why some may or may not be available to you.

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Traditional IRA

An individual retirement account, or IRA, is an investment account that allows you to contribute money that is largely tax-deductible, depending on your adjusted gross income.

This type of plan typically invests in an assortment of financial products, such as stocks, bonds or mutual funds, on your behalf. If your contributions are deducted from your paycheck, they reduce your taxable income. However, when you reach retirement age, withdrawals are taxed as income.

Pros	Cons
You can contribute up to $5,500 per year up to age 50, and $6,500 per year if you are 50 or older.	Account withdrawals during retirement are counted as income and taxed by the IRS.
The additional contribution limits for savers older than 50 allow for "catch-up" contributions.	Annual contribution limits are relatively low: $5,500-$6,500 per year.
Contributions for single/head of household individuals with an AGI of $63,000 or less are tax deductible.	You may face penalties for withdrawals prior to age 59 ½ or if not used for a qualified purpose—home purchase, qualified higher education expenses, certain major medical expenses, or certain long-term unemployment expenses.
There is a partial deduction for those earning an AGI between $63,000 and $73,000.	

Roth IRA

Roth IRAs are similar to traditional IRAs, except the contributions are not tax-deductible and do not reduce taxable income. However, qualified distributions made during retirement are tax-free, and investment gains are not counted as capital gains.

> *"An individual retirement account, or IRA, is an investment account that allows you to contribute money that is largely tax-deductible, depending on your adjusted gross income."*

Pros	Cons
Because you pay the tax up front, all the earnings grow income-tax-free.	You pay taxes up front.
Distributions are not taxed, as long as you are 59 ½ and account has been opened for 5 years	The maximum contribution is low—$5,500 per year in 2018. If you're 50 or older, you are allowed an additional $1,000 catch-up contribution each year.
This plan doesn't require minimum distributions.	Roth IRAs are typically not offered by your employer, so you usually have to set it up yourself.
Traditional IRAs require you to take distributions at age 70 ½; Roth does not.	You have to remember to fund it each year or set up automatic contributions from your bank account.
For the time being, you can leave your account to your heirs to potentially realize tax-free distributions over their lifetimes. Keep in mind that Congress may change that rule.	There are income limits. Phase-out starts at $120,000 per year, and you are ineligible at $135,000.
You can withdraw your contributions (but not your earnings) without penalty.	Future tax laws can change at any time and may impact the benefits of Roth IRAs. Their tax treatment may change.
You get tax diversification in retirement.	
Roth allows you to alternate distributions from each account so you don't inadvertently push yourself into a higher tax bracket.	
There's no income limit on converting your traditional IRA to a Roth, however, the converted amount is generally subject to income taxation.	

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SIMPLE IRA

A SIMPLE IRA, or Savings Incentive Match Plan for Employees Individual Retirement Account, is a defined contribution savings plan popular with small business employers and the self-employed.

The administration of this type of account is less complicated than traditional retirement plans such as 401(k), and it is not subject to Employee Retirement Income Security Act (ERISA) compliance. Like other retirement savings plans, it can be funded with pre-tax dollars.

Pros	Cons
SIMPLE IRAs are easy to set up and administer (no nondiscrimination testing or form 5500 filing).	There is a required employer contribution of a minimum 3 percent match or 2 percent non-elective contribution.
These plans allow for both employer and employee contributions.	Employee contribution limits are relatively low at $12,500 annually and a $3,000 catch-up for 2018. (2)
	Employer contributions must be 100 percent immediately vested.

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SEP IRA

A Simplified Employee Pension Individual Retirement Account (SEP IRA) is an IRA option meant for business owners to provide retirement benefits to themselves and their employees.

SEP IRAs are available to a variety of small-business types, including sole proprietorships, partnerships, LLCs, S corporations, and C corporations. Contributions are made to a standard IRA or annuity set up for each enrolled employee. If you are self-employed and have employees, they must all receive the same benefits under an SEP plan. In addition, SEP IRA funds can be invested the same way as most other IRAs.

Pros	Cons
SEP IRAs are easy to set up and administer, with no IRS Form 5500 filing required for most employee benefit plans.	These plans allow employer contributions only; employee contributions are not permitted.
These IRAs offer greater flexibility in plan selection compared to most IRAs.	Employers must contribute equally for all eligible employees.
Contribution limits are relatively high—up to 20 percent of net income up to $55,000.	You must take mandatory withdrawal by age 70 ½.
Employer contributions are flexible, with no fixed formula.	No catch-up contributions are permitted.
The minimum age to take withdrawals penalty-free is 59 ½.	

401(k)

A 401(k) plan is an employer-sponsored retirement account whereby eligible employees can make salary-deferred contributions on a pre-tax or post-tax basis. The plan was established in 1978. As of September 2017, 401(k) plans had about $5.3 trillion (3) invested in them nationally.

> *"401(k)s offert significant flexibility as to eligibility, employer contributions, plan selection, and vesting."*

Pros

High maximum employee contribution limit of $18,500 and up to $6,000 catch-up for 2018.

Employees can contribute as pre-tax, Roth, or a combination of both.

Many employers offer matching contributions

401(k)s offert significant flexibility as to eligibility, employer contributions, plan selection, and vesting.

Employees are typically eligible to take loans and hardship withdrawals.

The overall limit on contributions from all sources—including employer match—is $55,000.

Cons

401(k)s can be complex to administer, depending on the variety of plans offered.

Income is taxable when withdrawn during retirement.

You will face penalties for early withdrawal—20 percent taxed plus and additional 10 percent if you withdraw money before age 59 ½.

Sometimes employers require long waiting periods before contributions can begin.

Withdrawals are required at age 70 ½.

Solo 401(k)

Solo 401(k)s are like their corporate-sponsored counterpart, except that they are generally geared toward self-employed workers, such as freelancers.

There are stricter guidelines to follow than there are with a company-sponsored 401(k). For example, you may not be eligible if you work for an employer by day and work for your own company in the evening. In addition, the business's employees can consist at most of yourself and a spouse.

You also have to file an employer identification number (EIN) with the IRS, but if you qualify for a Solo, you can sock much more money away than you could via a company-sponsored 401(k).

Solo 401(k)s allow for two types of contributions: elective deferrals and employer contributions. With type 1, you can do elective deferrals up to $18,500 annually, or $24,500 if you are over age 50. For type 2, you can also make employer non-elective contributions up to 25% of compensation. Total contributions cannot exceed $55,000, or $61,000 if you are over age 50.

Pros	Cons
You have complete control over the 401(k) you choose to invest in.	You need to apply for an IRS EIN tax identification.
There is some flexibility in your contribution approaches: Type 1 or Type 2.	You can't have any employees other than yourself and a spouse.
Contribution limits are high—up to $55,000 annually.	
You can roll contributions from a 401(k), 457(b), 403(b), IRA, or Roth IRA into your solo 401(k) plan.	

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Profit Sharing

Profit sharing is an interesting form of retirement plan because it is essentially a variable pay plan, meaning company leaders designate a percentage of annual profits to be shared with employees.

Pros	Cons
When the company is doing well, you have the potential to participate.	Individual employees may not see how their own work and actions impact the profitability of the company. Consequently, while employees enjoy receiving their profit sharing money, it may become more of an entitlement than a motivational factor. (5)
Employers can choose how much to distribute each year, including making no contributions.	In 2018, the maximum contribution amount for a profit sharing plan was the lesser of 100% of compensation or $55,000. Thus, the amount of your compensation that can be taken into consideration when determining employer and employee contributions is limited.
The potential positive impact of profit sharing is that it sends the message that all of the employees are working together on the same team (4) and toward shared goals.	

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403(b)

The 403(b) plans are similar to 401(k)s in the way they work, but they are typically only offered to employees of public schools, some nonprofit organizations, and some religious ministers.

If you are self-employed, you can contribute as much as 25 percent of your net earnings up to $55,000, which can add up to a significant tax savings in the years you contribute.

Pros	Cons
Contributions are tax-deductible and reduce annual taxable income.	Offerings for plan participants are limited when it comes to where you can invest money.
No income tax is paid on interest earned while the plan grows.	This plan is only offered to certain types of employees.
Some individuals qualify for tax credit based on deferred income into a 403(b).	Contributions are limited to $18,500 per year as of 2018 with a total contribution from all sources limited to the lesser of $55,000 per year or 100 percent of employee's most recent annual salary.
Your employer may match contributions, depending on policies where you work.	Early withdrawals are subject to tax penalties similar to those associated with 401(k)s, except for qualified hardships, etc.
One of the biggest advantages of a 403(b) is that it reduces your taxable income. In 2018, you can put up to $18,500 into your plan; if you are 50 or older, that limits extends to $23,500.	

457(b)

Like a 401(k), a 457(b) plan is a type of nonqualified, tax-advantaged, deferred-compensation retirement plan that is available for governmental and certain non-governmental employers in the United States. It is also sometimes offered to high-paid ("top hat") executives at nonprofit organizations.

> *"Unlike with a 401(k), you will not pay the 10 percent penalty to withdraw 457(b) money when you leave your employer, however, income taxes may apply."*

Pros	Cons
Contributions to a 457(b) are taken from your gross income, reducing your taxable wages.	The 457(b) is offered to public sector employees only.
Unlike with a 401(k), you will not pay the 10 percent penalty to withdraw 457(b) money when you leave your employer, however, income taxes may apply.	A participant in a 457(b) plan is allowed to contribute up to 100 percent of annual gross income, but not more than $18,500 per year.
There is a high maximum employee contribution limit of $18,500 and up to $6,000 catch-up for 2018.	457(b) employer matches are relatively rare.
Some employers offer a catch-up contribution three years before retirement age of twice the annual limit, or $37,000.	For "Top Hat" plans, you may only roll over 457(b) money into another 457(b), not into an IRA, a 401(k), or a 403(b).
Employees can contribute as pre-tax, Roth, or a combination of both.	
Many employers offer matching contributions.	
This plan offers high flexibility as to eligibility, employer contributions, plan selection, and vesting.	

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Defined Benefit

A defined benefit pension plan is a pension plan that provides employees with a specific amount of retirement benefit based on the number of years of service that they have provided their company. At retirement, many plans allow the employee to choose how benefits are paid. Common payment options include some kind annuity or a lump-sum payment.

> *"You're covered up to a certain annual maximum by Pension Benefit Guaranty Corporation (PBGC) insurance. Companies are required to pay a certain amount of money for each pension they administer so if something happens to the company, PBGC rules require that employee pensions are covered by insurance."*

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Pros

- This type of retirement plan offers fixed benefits; you know exactly how much money you are going to get when you retire.
- If you work past retirement age, you may be eligible for a possible increase in payout.
- This plan offers high annual benefit limits—100 percent of your average compensation for the highest three consecutive calendar years, up to a maximum of $220,000.
- You're covered up to a certain annual maximum by Pension Benefit Guaranty Corporation (PBGC) insurance. Companies are required to pay a certain amount of money for each pension they administer so if something happens to the company, PBGC rules require that employee pensions are covered by insurance.
- You know exactly how long you need to work in order to retire.

Cons

- You may not be able to make as much money as you would have been able to with a defined contribution plan such as a 401(k).
- You do not have any control over your investments.

Thrift Savings

A Thrift Savings Plan, or TSP, is a tax-deferred retirement savings and investment plan offered to federal employees and structured with the same type of savings and tax benefits offered by private companies to their employees under 401(k) plans.

A TSP plan allows federal employees the opportunity to save part of their income for retirement, receive matching agency contributions, and reduce their current taxes. However, the fund selection is highly limited.

Government employees can choose from the following options: the Government Securities Investment (G) Fund, the Fixed Income Index Investment (F) Fund, the Common Stock Index Investment (C) Fund, the Small Capitalization Stock Index Investment (S) Fund, the International Stock Index Investment (I) Fund, and specific life cycle (L) funds—sometimes called target date funds—designed to manage risk based on your anticipated retirement age. The principal value of target date funds is not guaranteed at any time, including at the target date.

Pros	Cons
You can take a loan out to purchase items such as a primary residence.	Only federal civilian employees are eligible.
You have in-service withdrawal options under certain circumstances.	The catch-up contribution limit for employees age 50 and over is $6,000.
This plan comes with low administration and investment costs.	Investment choices are limited—only six different funds are offered.
	You lose the ability to contribute after your government service ends.
	This plan is administered by a government agency, as opposed to corporate employer.

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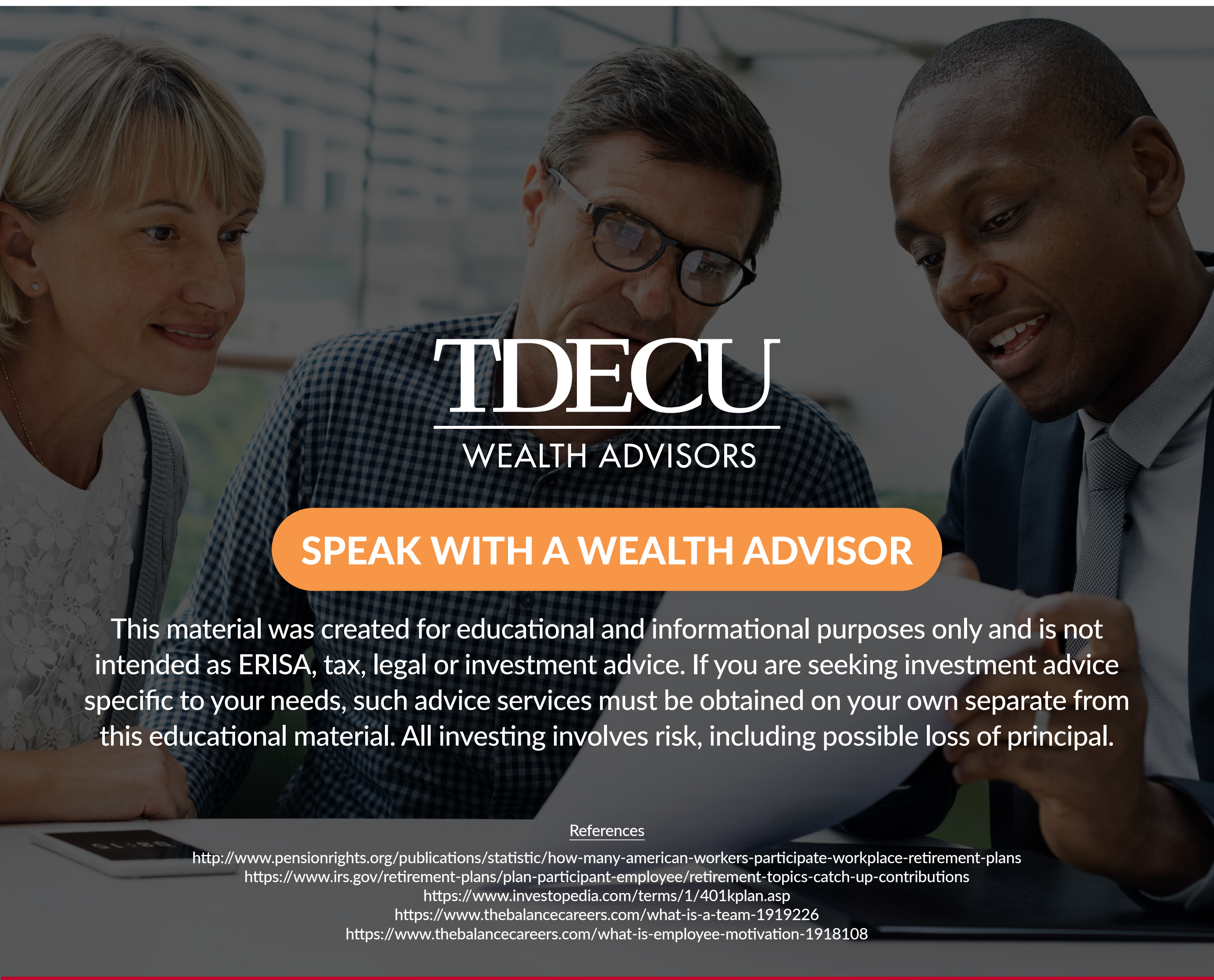
Conclusion

There are many different ways to invest and save for retirement. However, many of the plans currently offered either through work or the open market have complicated rules that must be followed in order to maximize return potential and avoid penalties.

The highlights and downsides of the preceding plan descriptions should make it easier to select the type of investment that is right for you as you save your retirement nest egg.



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