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From the Baltimore Sun

Roth can top regular IRA

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Kevin, of Towson, is building his retirement nest egg and trying to decide between two investment options.

The 28-year-old has a tax-deferred retirement plan at work, but there's no employer match.

He has been advised to put his money into a Roth IRA. But he wonders whether the Roth is worthwhile if he's able to contribute money for only a few years before his rising income makes him ineligible.

What if he has, say, \$10,000 in the Roth and then no longer can contribute? "Although I won't be taxed on whatever that compounds to when I'm 60, it doesn't seem like it would be worth it," he e-mailed.

It took T. Rowe Price Associates' financial planner Stuart Ritter a second to come up with the answer: "Use the Roth."

Rates may rise

Younger workers such as Kevin can contribute \$4,000 a year to a Roth. Contributions begin phasing out at \$95,000 for singles and \$150,000 for married couples. The money goes in after taxes have been paid on it, and withdrawals are tax-free in retirement. And there's a chance that tax rates will be higher in the future, making tax-free withdrawals even more valuable.

Here's the math:

Say Kevin has \$10,000 now in his employer's plan and \$10,000 in a Roth. No additional contributions are made for the next 32 years. When Kevin is 60, the after-tax value of the Roth would be \$87,153; the value of the tax-deferred account would be \$79,247. That's assuming Kevin's income tax rate is 25



percent today and will be the same in the future. And that he earns an annual return of 7 percent on his money.

Workers can look at their own situations using Price's online IRA calculator at www.troweprice.com. (The tax-deferred, no-match retirement account is the equivalent of a traditional, deductible IRA.)

On the other hand, what if Kevin gets a job with an employer that provides a match? Given Kevin's youth, Ritter says, he should first contribute enough to the employer plan to get the match and then put extra money away in a Roth. •

Fay of Dallas asks: What do you do with a 401(k) when you leave one job for another?

Workers have several options. And the last one should not really be an option at all.

First, leave the money in the employer's plan. It's easy. And this may be attractive to those who like the investments in their plans. The drawback: Workers forget about the accounts or don't monitor them, says Doug Robinson, a planner in Bel Air.

Not all companies, though, want ex-employees in the plan, particularly when accounts are small. In these cases, the company can cut a check for accounts under \$1,000 when the former employee doesn't take any action to have the money transferred elsewhere, Price's Ritter said. For accounts of \$1,000 to \$5,000, the employer would have to roll the money into an IRA. The employer must allow accounts of \$5,000 or more to remain, Ritter says.

The second option: Roll the money into a new employer's 401(k), if the plan permits. The advantage is simplicity. "You only have one pot of money to worry about managing and tracking," Robinson says. Investment choices are limited to whatever is in the plan, though.

Costly option

Or, you can have your account rolled directly into an individual retirement account. Financial planners usually recommend this because workers have a broad selection of investments and more control over their money. But too much choice may overwhelm.

Last, you can cash out the account. But this option comes at a high price and is ill-advised. You'll owe ordinary income tax on the money. Plus, if you're younger than age 55, you'll be hit with a 10 percent early-withdrawal penalty.

Not only that, you'll likely spend money today that was intended for tomorrow's retirement. And it will take a long time to build up the savings again.

Questions? Comments? Write personal.finance@baltsun.com.

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