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How To Save For Your Retirement At Every Age

When should you start saving for retirement? There's no time like the present, whether you're fresh out of school or in the middle of your career. And even if you haven't been able to set aside much, if anything, during your main working years, realize that it's never too late to begin.

Of course, you're more likely to secure a comfortable retirement if you can save consistently over your lifetime. Keeping that in mind, here's an overview of what you might do during different stages of your life.

Ages 20-40: It makes sense to get in on the ground floor when you can. For many people, the best place to start is with a 401(k) plan or another such employer-sponsored retirement plan that offers substantial tax advantages.

For instance, if you're eligible to participate in a 401(k), you can defer up to $18,000 to your personal account in 2016. (This figure is indexed for inflation annually and may be adjusted upward.) Your contribution isn't taxed now. Your employer may provide matching contributions, too, based on how much you put in. So if you're eligible and not actively participating in your company's plan, you're leaving money on the table.

But don't stop there. If possible, supplement your 401(k) or similar plan with an IRA or other kind of saving plans. With a traditional IRA, your contributions may be wholly or partly tax-deductible. Then, as with a 401(k), money withdrawn during retirement is generally taxable. With a Roth IRA, you can't deduct contributions, but future distributions are generally exempt from tax.

Starting to save early in one or more of these retirement plans puts time on your side, and the power of tax-deferred investment compounding can be formidable. Suppose you're age 30 and plan to retire at 67. Let's assume that you earn $100,000 a year and contribute 5% to your 401(k), while your employer provides an annual 50% match of 3% of your salary. If you earn a hypothetical return of 7% annually on account funds, your yearly contributions of $5,000, bolstered by your employer's $1,500, will grow to $1,081,038 by the time you're ready to retire.

Of course, this is a busy time of life, and the cost of buying a house and starting a family, among other expenses, could affect how much of your income you can earmark for retirement savings. But if you can manage to save regularly and steadily, the potential payoff could be substantial.

Ages 40-60: If you're able to sustain a sound retirement saving strategy that you began in your 20s and 30s, you'll be ahead of the game. But financial obligations during this 20-year stretch sometimes can be overwhelming. You might move to a larger home, expand your family, and shoulder part or all of the cost of putting your kids through college.

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Cash In On This Gift Tax Break For Section 529 Plans

If you're worried about saving money for your children's college educations, you should investigate Section 529 plans. These tax-favored accounts enable you to sock away money that can grow without current taxes. And the funds you withdraw to pay most college costs are also exempt from income tax.

Section 529 plans are operated by states, and although each state has its own ceiling for contributions, most limits are well into six figures.

But there's one catch. When you contribute money to a Section 529 account on behalf of a child or grandchild, the transfer is subject to gift tax rules. The current annual gift tax exclusion is $14,000 per recipient, or $28,000 for a joint gift by a married couple. If you give more than that amount, the excess will reduce your lifetime exemption from gift and estate taxes.

Fortunately, tax rules let you make a one-time contribution to a 529 plan that is treated as if you gave the money over five years. Thus, you can provide the equivalent of five years' worth of contributions in one year—so, up to $70,000, or $140,000 from a couple—without gift tax issues. You won't be able to give additional funds for five years without affecting your gift and estate tax exemption, but even those amounts might cover most or perhaps even all of a beneficiary's education costs.

Don't forget about this unique gift tax break when planning how to meet college expenses.

Do Robo Advisors Have Glitches?

Robots already do serious work in manufacturing, construction, and an increasing number of other fields. And now, "robo advisors" are invading financial services. Within the next decade, these automated portfolio managers are expected to be handling trillions of dollars in assets.

But are robo advisors an upgrade over their human counterparts? The jury is still out on that question, so let's take a closer look.

How do robo advisors work? It's not like R2-D2 sets up a face-to-face meeting at his office and devises a financial plan for your future. Instead, you input critical data—including your age, risk tolerance, assets, and goals—into a software package, which then spits out an investment "asset allocation" based on an algorithm. So, the technology does all of the grunt work.

Typically, the allocation will rely heavily on exchange-traded funds (ETFs) holding a mix of domestic and international stocks and bonds. Although robo advisors vary, normally the algorithms that determine which ETFs to hold are based on modern portfolio theory or a version of it.

Although you may be attracted by the idea of a portfolio automatically tailored to your needs, robo advisors have certain shortcomings. For one thing, they haven't been sufficiently tested during a range of market conditions such as the sustained downturn that began in 2008-2009.

In addition, there's the fact that a faceless, mechanical robo advisor won't react in the same way as a human advisor. Who is responsible if your investments go south? You can't consult with the tech experts who provided the coding for the software (nor are they likely to know much about managing your investments). In some cases, there is an 800 number you can call, but the software still drives the final decisions.

Furthermore, a robo advisor operates in a virtual vacuum. It doesn't have a complete financial picture or know you personally. If there's a call center for a particular robo advisor, you'll likely speak to a different person every time you call. In other words, the methodology behind these technological marvels won't take into account all of the factors influencing your life.

Finally, proponents of robo advisors claim that they are less expensive than human advisors, but that's not always the case. In any event, you may find that the services of a trusted personal advisor are well worth the cost in the long run. Despite the latest technological advancements, humans can still play a valuable role in guiding your investment decisions. ●

DOL Approves Final Fiduciary Rule

At long last, the controversial "fiduciary rule" for retirement accounts has been approved, with some modifications, by the Department of Labor (DOL).

The fiduciary rule drew a firestorm of criticism when it was first proposed in 2015. After lengthy hearings and thousands of comment letters from the public, the DOL went back to the drawing board. The final rule that has emerged takes into account some concerns that were raised, but keeps the basic framework intact.

Under the final rule, firms providing investment advice pertaining to retirement plans and IRAs must put their clients' "best interest" before their own. Essentially, financial advisors can't receive compensation without qualifying under the Best Interest Contract Exemption (BICE). Otherwise, their actions may constitute "prohibited transactions."

The new final rule clarifies the rules for the BICE by establishing a contractual fiduciary duty between investors and financial advisors. To qualify under the BICE, fiduciary standards of conduct must be acknowledged in a written contract.

In that contract, advisors must state that the advice they offer is based on a client's particular needs. This includes recommendations relating to a retirement plan, a plan participant or beneficiary, a plan fiduciary, or an IRA owner in exchange for fees or other compensation—for buying, holding, selling, or exchanging investments. It also covers advice on rollovers, transfers, and distributions from plans and IRAs. The fiduciary standards also cover disclosures on reasonable compensation, costs of providing advice to clients, and conflicts of interests.

The final rule also establishes what is ***not*** advice for these purposes. General communications such as financial newsletters, marketing

Five Big Tax Penalties To Avoid At All Costs

Taxes are a necessary evil, but you don't want to make matters worse by paying unnecessary federal tax penalties. Here are five to avoid:

1. Not taking required minimum distributions. This is the granddaddy of tax penalties. After you reach age 70½, you must begin taking annual "required minimum distributions" (RMDs) from your tax-advantaged retirement plans (unless you're still working) and from traditional IRAs. (For the year you turn 70½, you can postpone the payout until April 1 of the following year, but that will require you to take two withdrawals in the same calendar year.) The RMD is based on your age—entered into a life expectancy table—and your account balances at the end of the year in which you turn 70½.

Failing to take RMDs can result in a 50% penalty tax on the amount that should have been withdrawn (on top of the regular income tax you owe on the distribution). Unless you can show reasonable cause for missing an RMD, you'll be stuck with this penalty.

2. Making early withdrawals. On the opposite end of the spectrum, you may be penalized for withdrawing funds from your qualified plans and IRAs too soon. Generally, a 10% penalty tax applies, in addition to the regular tax you owe on the distribution, unless you've already reached age 59½ or the payout is because of death or disability. However, the tax law provides several exceptions to the early withdrawal penalty, such as payments used for deductible medical expenses.

Another key exception is available for substantially equal periodic payments (SEPPs). If you take SEPPs over your life expectancy, or over the life expectancy of you and a beneficiary or beneficiaries, there's no penalty if those payments continue for at least five years or until you reach age 59½, whichever is longer.

3. Not reporting income from foreign accounts. Your tax return may not be the only document you're required to file each year. If you have financial interests in foreign banks totaling more than $10,000 at any time during the year, you must report the account information to the IRS using the FBAR form (short for Report of Foreign Bank and Financial Accounts).

FBARs have to be filed by June 30 of the year following the year of the foreign account activities, and no extensions are allowed. (Beginning with the 2016 tax year, the FBAR deadline is moved up to April 15 and a six-month extension is available.) The penalty for failing to make the filing is severe—a fine of up to $250,000 and a prison sentence of up to five years can be assessed for a willful violation. Other penalties may be imposed for providing false information.

4. Not having health insurance. Under the Affordable Care Act (ACA), also known as Obamacare, most people must have health insurance or must pay a "shared responsibility payment." For 2016, the amount of that payment is equal to the greater of 2.5% of your annual household income or $695 per person for the year ($347.50 per child under 18), up to a maximum of $2,085 per family.

This penalty kicks in when you, your spouse, or a dependent go without coverage for more than three months, with certain exceptions. Consult with your tax and financial advisors to see whether you qualify for a premium tax credit or an exception to the penalty.

5. Missing the deadline for your tax return. Generally, if you don't file your tax return on time, or if you fail to pay the tax you owe by the tax return due date (even when you receive an extension for filing your return), you'll be assessed a penalty.

The penalty for filing late is 5% of the unpaid taxes for each month or part of a month that a tax return is late. It begins accruing after the tax-filing due date and can't exceed 25% of your unpaid taxes. If you don't pay your taxes by the tax deadline, you normally face a penalty equal to 0.5% of the unpaid taxes. This applies for each month or part of a month after the due date and starts accruing the day after the tax-filing due date.

Again, the six-month filing extension, which is automatic if you request it, is not an extension for *paying* your taxes. You still must make a reasonable estimate and pay that amount. ●

materials, and educational materials don't count.

A main difference between the final rule and the earlier proposed version is that additional financial products, including variable annuities and private placements, are now included under the BICE. The final rule also eliminates a requirement for financial advisors to give clients an annual transaction disclosure on costs. Another key change wipes out the need for advisors to provide regular projections of fees over one, five, and 10 years.

Finally, the process of implementing the BICE is streamlined. Now a contract can be completed when a client opens an account.

For most advisors and clients, the final rule takes effect on April 10, 2017, although in some cases the effective date will be January 1, 2018. More details will be forthcoming. ●

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How To Save At Every Age

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However, if you can keep saving, your retirement plan and IRA contributions will continue to bolster your nest egg during a time when your job income may rise substantially. You can continue IRA contributions even if they're nondeductible. Moreover, once you reach age 50, you can make "catch-up" contributions that increase the maximum amount you can put in a 401(k) each year. The maximum catch-up contribution for 2016 is $6,000. (This figure, too, is indexed annually for inflation.) These extra amounts can help you make up for lost ground once you've paid those college tuition bills. Depending on your situation, you also might decide to convert traditional IRA funds to a Roth IRA. You'll owe current taxes on the amount you convert, but you may secure tax-free payouts in retirement.

Furthermore, if you can manage to pay off your mortgage during these years, you could earmark the money that had been going for monthly loan payments to increase the amount you put away for retirement.

Ages 60 and up: Now is the time for a final savings surge. Be sure to maximize retirement and IRA contributions, and set aside extra money in other accounts if you can.

At the same time, consider several crucial decisions that could affect your retirement lifestyle. One very important question is when to apply for Social Security benefits. For most Baby Boomers, full retirement age (FRA) is age 66, but it gradually increases to age 67 for younger people. If you apply before you reach FRA, as early as age 62, you'll receive lower monthly benefits. Waiting longer, until as late as age 70, will produce higher benefits. Other decisions about Social Security may affect married couples.

Another decision involves your home. Downsizing to a smaller, cheaper house, perhaps in an area with lower costs, could help you minimize your expenses as you approach retirement.

Finally, remember that retirement planning doesn't end when you retire. It's an ongoing process, and from now through the rest of your life, you'll probably need to make periodic adjustments to your investment strategy and your plan for tapping your savings. ●