

Focus on Funds: Maximize Your Tax Savings with Individual Retirement Accounts

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There's still time to cut your 2019 tax bill by opening or contributing to an individual retirement account (IRA). In the April 3, 2020, edition of *Focus on Funds*, ICI Senior Director of Retirement and Investor Research Sarah Holden breaks down the options.

Transcript

Stephanie Ortals-Tibbs, ICI director of media relations: As tax filers well know, the IRS deadline is coming up. And there's something smart you might want to add to your tax to-do list before then. Sarah Holden, one idea is to just make sure that, if you haven't already, you contribute to or open up an IRA (an individual retirement account).

Sarah Holden, ICI senior director of retirement and investor research: This is a perfect opportunity to open or contribute to an IRA because you can count the contribution as having occurred last year. And if you're able to take a deduction, this could actually have an impact on your taxes that you owe.

Ortals-Tibbs: Definitely worth paying attention to, then. And there are a number of choices you can make; walk us through those.

Holden: Really, the key first choice is whether you want to open a traditional IRA or a Roth IRA. And the difference there is in the tax treatment. With a traditional IRA, if you're able to take a deduction, then you don't pay taxes on the contribution now. So you get a tax break now. Once the money's in the account, it compounds and grows tax-free. But when you get to retirement and you withdraw the money, it then gets counted as part of your income, and you pay the taxes on it then.

With a Roth IRA, on the other hand, it's an after-tax contribution, so you don't get a tax break today. But the money grows and compounds tax-free, just as it did in the traditional IRA. And when you get to retirement and take the money out, because you paid the taxes up-front, you don't owe any additional taxes.

Ortals-Tibbs: So if I'm the average person, I'm trying to think which one of these would appeal to me. What should I be keeping in mind?

Holden: So what we see in the data is that a lot of younger investors are attracted to the Roth option. Because if you think about it, you're younger; you're at the beginning of your career; you're probably in a low tax bracket. So that tax break today isn't as important

to you, and you'd rather have it later. We also hear that [when] some people do it, they're thinking ahead to retirement. And in retirement, when you're taking money out of your IRA, it might be nice to have the Roth IRA for those what we call "lumpy expenditures." And if the roof on the house needs to be fixed, or you need to get a new car, you need to take out more money. If you have a Roth IRA, you can take that extra money out, and it has no impact on your taxes.

Additional Resources

- [10 Important Facts About IRAs](#)
- [ICI Explains: Who Invests in Mutual Funds, and Why?](#)
- [IRA Resource Center](#)

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