

Roth IRAs: A Flexible Approach to Building Assets



Many workers who wish to save for retirement, homeownership, or other purposes may find that the Roth Individual Retirement Account (IRA) is an attractive way to save that offers important advantages. It can be an effective alternative for workers unable to obtain an Individual Development Account.

In a regular savings account, the interest earned on the account counts as taxable income. The interest earned in a Roth IRA, in contrast, is normally not taxable. In fact, all funds in a Roth IRA may be withdrawn tax-free so long as the account is at least five years old and:

- the worker has reached age 59½; or
- the worker or the worker's spouse, child, or grandchild is using IRA funds for a first-time home purchase (up to \$10,000 toward each purchase); or
- the worker is using IRA funds for higher education expenses; or
- the worker is disabled.

Roth IRAs also have several advantages over traditional IRAs. Most notably, withdrawals from traditional IRAs are taxable, while withdrawals from Roth IRAs aren't. In addition, traditional IRAs have substantial penalties for withdrawal before age 59½. (While there are exceptions, any early withdrawals still count as taxable income.) Traditional IRAs also require holders to begin withdrawals at age 70½, while Roth IRAs have no mandatory withdrawals at any age and also allow contributions after age 70½.

The main benefit of traditional IRAs is that workers can deduct the contributions to these accounts from their income, reducing their income tax liability. Roth IRAs do not provide this benefit. However, many low- and moderate-income workers — such as those who qualify for the EIC — don't need this tax advantage, either because they don't earn enough to owe income taxes or because they do owe income taxes but don't need an additional deduction.

While some workers may feel they don't earn enough to put any money aside for retirement, their EIC or CTC refund may provide enough funds to establish a Roth IRA. Minimum deposits to start a Roth IRA can be as low as \$100. Roth IRAs can be established as bank certificates of deposit and other investment products. In 2011, workers can contribute up to \$5,000 to a Roth IRA; this limit is \$6,000 for workers over age 50.

Organizations Can Provide Counseling on Roth IRAs

The Financial Clinic partners with United Way of New York City to provide tax assistance and financial development services to low-income families during tax filing time. The Financial Clinic begins with basic financial education on building savings, improving banking and credit, debt management and tax planning through a thirty question survey. Filers are invited to take advantage of further financial coaching activities including advice on how filers can use a part of their refund to start saving for retirement. Filers are provided with easy-to-read TipSheets that explain the differences between IRAs and Roth IRAs. One of its most effective techniques is for tax preparers "to do the math" with the filers by demonstrating how small, consistent contributions today benefit them decades later. Participants continue to receive year-round financial coaching, which assists them in following their savings plans and managing their retirement accounts outside of the tax season. *For more information on how these practices can be integrated into tax preparation, please contact Haidee Cabusora, The Financial Clinic, hcabusora@thefinancialclinic.org.*

Some workers who contribute to IRAs can also claim tax benefits. See "[Saver's Credit](#)" in the *More Facts About Tax Credits* section at www.eitcoutreach.org.