FEMALE FINANCE

NO 401(K)? NO PROBLEM!

Here's a Retirement Plan for the Rest of Us

By Elizabeth Lewin

Do you have a retirement plan or pension where you work? If you don't, you're not alone: 28 percent of women don't have a retirement plan on the job—and those who do receive roughly half the amount that men do. So what's a woman without a plan to do about retirement? If you're married, you may be able to count on your husband's plan distributions, and there's always Social Security, of course: 50 percent of all women collecting Social Security rely upon it for at least 90 percent of their income, compared with 29 percent of men.

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But neither of those options is a *good enough* plan. Given the recent dire predictions about Social Security—and the considerable insecurity about how it may be changed in the future—MAKING BREAD decided this might be a good time to put together a fool-proof plan for the rest of us—the millions of women who don't have 401(k) plans or pensions on the job. Never fear. There are still several good ways to save for a secure retirement.

Don't Be Shy & Retiring About Saving for Retirement

Start with that old stand-by, the traditional IRA. Whether you are a working mom, a stay-at-home mom, single, married, or divorced and collecting alimony, opening an Individual Retirement Account should be your first move towards financial security.

The maximum amount you can contribute has increased from $3,000 to $4,000 for 2005. If you turn 50 this year, you get a birthday present—an extra $500 allowable contribution for those 50 and over, bringing the maximum up to $4,500. No matter what your age, your contribution may be tax-deductible. The deductibility of IRA contributions depends on income (your adjusted gross income can't exceed $50,000 for singles or $70,000 for marrieds filing jointly) and whether you have a retirement plan at work. If you are not eligible for a tax-deductible contribution, you can make contributions up to the same dollar limit, anyway. You won't get the deduction, but your contributions grow on a tax-deferred basis.

IF YOU DON'T HAVE A 401(K), MAX OUT YOUR IRA!

Tax Year	Max for Under 50s	Max for 50-Plus
2000-2004	$3,000	$3,500
2005	$4,000	$4,500
2006-2007	$4,000	$5,000
2008 onward	$5,000	$6,000

Those not eligible for a traditional tax-deferred IRA on the basis of their income should consider a Roth IRA, where the income limits are higher: $110,000 for single filers and $160,000 for marries filing jointly. Contributions aren't deductible, but earnings are tax-free.

If you qualify for a tax-deductible IRA, you'll have to decide which is the better type for you: a plan that offers you a tax deduction now (a traditional IRA) or one that offers a tax-free withdrawal later (a Roth IRA) rather than a tax deduction today. There is no easy answer, of course: you have to consider such factors as your age, your current income, and your expected tax brackets during your working and retirement years. To help you crunch the numbers, use the IRA calculator at www.MyFICO.com. As a rule of thumb, you'll do better with a Roth IRA if you expect to be paying a substantially higher rate of tax after retirement than you are currently paying right now.

You can contribute to both a traditional and a Roth IRA—if your income doesn't exceed the limit—but total annual IRA contributions must not exceed the amounts in the box above.

Some other points to remember:

- If you are not covered by any pension plan, you can make an IRA contribution that is fully tax deductible, regardless of income.
- If either you or your spouse are not working, the employed spouse can contribute to an IRA in the other spouse's name. For the 2005 tax year, a stay-at-home spouse can stash up to $4,000 in his or her own account. Regardless of who makes the contribution, it's the person whose name is on the account who has control of the dough. To protect yourself, just in case you end up splitting up, make sure that your spouse opens the account in your name.
- The self-employed and small business owners should look into various types of IRA's and other tax-deductible plans created especially for them. They include Simple IRA's, in which the maximum contribution is $8,000 annually; Keogh Plans, which allow a contribution of up to 20 percent of adjusted compensation to a maximum of $40,000; SEP-IRA's, in which your contribution is limited to 25 percent of earned income to a maximum of $40,000; and self-employed 401(k) plans, in which you can contribute up to $12,000 per year.

Next, park some money in an HSA. Health Savings Accounts (HSA's) do double duty: they provide virtually all workers under age 65 a means of saving money on a tax-deductible basis to pay for medical expenses and retirement.

Here's how they work: A Health Savings Account is like an IRA. You open one at a financial institution, in conjunction with an HSA-approved high deductible health plan (HDHP)—one with an annual deductible of at least $2,000 for a family ($1,000 for an individual). Once your insurance policy has →

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become effective, you may fund your HSA account.

The maximum amount that can be contributed and deducted from your Federal income tax is the lesser of the amount of your plan's annual deductible or the maximum specified by law (up to $5,250 a year for a family or $2,650 for an individual). Taxpayers, 55 and older, can contribute an additional $600 a year. These amounts are adjusted annually for inflation.

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Use the money in the HSA to pay your out-of-pocket medical expenses under your high-deductible health plan. In addition to covering deductible expenses under your HDHP, you may make tax-free withdrawals to pay for *medical* services not covered by your insurance, such as dental expenses, mental therapy, physical therapy, alternative treatments, transportation and lodging expenses, preventive health programs, prescription and over-the-counter drugs, special fees incurred by handicapped individuals, insurance premiums for long-term-care insurance, or to cover COBRA payments or health-insurance premiums in the event that you become unemployed. Visit the following Government Web site for complete information: www.ustreas.gov/offices/public-affairs/hsa.

If you are not covered by any pension plan, you can make an IRA contribution that is fully tax deductible, regardless of income.

Once you meet your plan's maximum out-of-pocket medical expenses, your high-deductible insurance policy kicks in and covers 100 percent of your medical costs. The money that you don't use each year just accumulates in your savings account toward future medical expenses or for your retirement. Earnings on your savings are tax-deferred. Withdrawals used to pay medical expenses are not taxed. However, if you withdraw money for non-medical purposes before age 65, you will have to pay income taxes and a 10 penalty.

After age 65, the HSA is treated as an IRA, and you can make withdrawals for non-medical reasons without penalty. These withdrawals are reported as ordinary income and taxed.

In the meantime, your money is invested in your choice of investment fund (either a savings account or in mutual funds, which have a higher potential return), and interest accumulates, tax-deferred. If you contribute the maximum amount each year to an HSA and enjoy good health much of that time, you will accumulate a sizable nest egg. How large an egg depends on the interest rate at which your investment grows and how much of your contribution is used to pay medical bills.

What should you do if have any money left over? You have several options to consider. For starters, there are annuities. A long-term investment, annuities are a place to stash your money if you've already maxed out your tax-deductible IRA or HSA. They make good sense if you have 10, 15, 20 or more years till retirement, if you are looking for a pretty sure thing, and if you expect to live a long, long time. The wild card in the deck is this: monthly payouts are based, in part, on life expectancy, so if you beat the odds, the insurance company loses and you come out ahead of the game.

All that being said, what exactly is an annuity, and how does it stack up against other retirement investments? Basically, it's an investment contract with an insurance company under which you pay the company a sum of money (the minimum is generally $5,000), and eventually receive a lump sum or periodic payout of the principal and interest earned. Interest rates on annuities are generally higher than those available for CD's. However, CD's are FDIC-insured and annuities are not. Still, most annuities protect your principal, and, in some cases, even guarantee a specified level of return.

Historically, the stock market has outperformed all other types of investments. Just remember to protect your posterior by diversifying; don't put all your savings in one basket.

Unlike 401(k) and IRA contributions, your investment is made with after-tax dollars. However, the interest it earns is reinvested and keeps on growing, tax-deferred, until it is withdrawn. You only pay taxes on the money you take out when you take it out. That means that, if you opt for monthly payments instead of a lump-sum payout, you can stretch the tax hit over the lifetime of the payout and, in many cases, you end up paying taxes on that money when you are in a lower tax bracket.

There's no limit on how much you can invest in an annuity, so if you've just received an inheritance or a divorce settlement, an annuity might be one place to stash it. Also, unlike an IRA or 401(k), You don't have to begin taking withdrawals (and paying taxes) at age 59 1/2. Two other advantages: in some states, annuities are protected from creditors, and, passed on as part of an inheritance, they can escape probate. Annuities are complex investments, with many options and consequences for both you and your heirs. Before buying, I recommend that you discuss your choices with a financial planner.

If you have a little more appetite for risk, your next best bet is investing systematically in the stock market. What do I mean by systematically? Make it automatic. Open up a mix of stock and bund mutual funds—or a balanced fund that invests in both stocks and bonds—and, just as you would if you had a 401(k) account, have a specified amount of money transferred from your paycheck each pay period and deposited directly into your fund(s). Investing in the stock market is like power saving—or saving on steroids. Though there is a certain amount of risk involved, there is also far greater potential for gain. Historically, the stock market has outperformed all other types of investments. Just remember to protect your posterior by diversifying; don't put all your savings in one basket. Diversification reduces risk.

Of course, the most obvious retirement investment may be the house that you're sitting in as you read this. Real estate is probably the best single investment available for most people. Home values have beaten the rate of inflation in the last eight years, and there are considerable tax advantages to owning a home: mortgage interest, points and property taxes are all deductible. A house purchased for $30,000 some 30 years ago could now be now worth $150,000 or more, depending on location. That's a 400 percent return on investment. Moral of that story: if you haven't bought a house already, start saving for one—and searching for a low-down-payment mortgage. Visit www.homepath.com for more information.

So, there you have it—at least five good ways you can save for your retirement, even if you don't have a 401(k) plan. No excuses. Start early and you will accumulate a comfortable nest egg for yourself. ■

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