
## Breaking Down IRAs

Individual retirement accounts (IRAs) are a type of tax-advantaged account that can help you boost your retirement savings. The most common IRAs you will choose from are traditional and Roth IRAs. Both are designed for long-term growth, but there are some key differences, including how your contributions are taxed and when you can withdraw funds. Here is a breakdown of the two accounts and a look at how to choose the one that is right for you.

**Traditional IRAs**

Anyone age 18 and older with an earned income can make contributions to a traditional IRA of up to $6,000 a year in 2021. Those age 50 and older can contribute up to $7,000. Contributions are tax-deductible, and your savings grow tax-deferred. You may begin making withdrawals at age 59 ½, and you must take required minimum distributions at age 72. Withdrawals are subject to income tax, and early withdrawals before age 59 ½ may be subject to a 10% penalty.

Your ability to deduct contributions to a traditional IRA is dependent on your income. Married couples filing jointly with a modified adjusted gross income (MAGI) of up to $105,000 can deduct the full amount, as can single filers with a MAGI of up to $66,000. If you exceed these income limits you can still make partial deductions until eligibility is phased out for singles making $76,000 or more and couples making $125,000 or more.

**Roth IRAs**

Contributions to a Roth IRA are made with after-tax dollars, and money inside the account grows tax-free. The annual contribution limit for a Roth IRA is also $6,000, or $7,000 for those age 50 and older.

If you are over age 59 ½, you can withdraw funds at any time and there are no minimum distribution requirements. Regardless of age, you can withdraw your contributions at any time without paying penalties or taxes. However, if you withdraw earnings before you reach age 59 ½, you may have to pay penalties and taxes. You may also need to pay taxes and penalties on withdrawals if you havee been making contributions to your Roth IRA for less than five years.

Only those with incomes less than $198,000 for couples and $125,000 for a single person can contribute to a Roth IRA. If you earn more than that, you can still make partial contributions if your income is $140,000 or less for a single person and $208,000 for married couples.

**Choosing which account is best for You**

The main difference between a traditional IRA and a Roth IRA is how and when contributions are taxed. You can deduct contributions to a traditional IRA and lower your taxable income for the year in which you made the contributions, but you will pay taxes on your withdrawals. Roth IRAs don't offer immediate tax benefits — you make contributions with after-tax dollars — but withdrawals are tax-free.

When choosing between the two accounts, the best choice for you likely depends on whether you think your tax rate will be higher or lower in the future. If you anticipate a higher tax rate in retirement, a Roth IRA may be the better choice, since withdrawals are tax-free. And if you expect a lower income tax rate in retirement, a traditional IRA can offer you more tax advantages since you can lower your taxable income now and pay a lower income tax rate on withdrawals in the future.

You don't necessarily have to choose between the two accounts; It is also possible to contribute to both. Contribution limits are cumulative across accounts, so total contributions cannot exceed $6,000 ($7,000 for those 50 and older) in 2021.

Whether you choose to fund a traditional IRA, Roth IRA or both, you'll be taking advantage of tax benefits that can supercharge your savings and bring you closer to achieving your retirement goals.

Sources:

https://www.irs.gov/retirement-plans/plan-participant-employee/retirement-topics-ira-contribution-limits

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https://www.irs.gov/retirement-plans/traditional-and-roth-iras

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