

Roth IRA + 401k=Roth 401k

Next year a new retirement plan may be available...a plan whose aim is decreasing your tax burden at retirement. Highly compensated employees and executives are the most likely people to take advantage of this new account since they have the most to gain.

To be specific, this new plan is the Roth 401-k. Quite simply, the Roth 401k is a combination of the tax benefits of the Roth IRA with the structure of the “traditional” 401k. People will be allowed to contribute *with after-tax dollars* to tax-deferred savings accounts in order to receive *tax-free withdrawals* at retirement. This differs from the Traditional 401-k in which contributions are made on a pre-tax basis but all withdrawals are taxed by local, state, and federal governments as ordinary income.

A recent study showed that 30% of employers surveyed were considering offering a Roth 401-k Plan in the next twelve (12) months (Hewitt Associates, Inc.).

How will the Roth 401-k Plan work?

The 2006 401-k contribution maximum is \$15,000, \$20,000 for people 50 and over. Therefore, workers will have 3 options: 1) contribute exclusively to their Traditional 401-k; 2) contribute exclusively to a Roth 401-k; or 3) split the contributions between the two accounts up to the stated maximums.

Who stands to benefit?

The Roth 401-k is an excellent plan for people whose tax brackets will be higher at retirement.

If the national debt continues to grow, Congress may need to raise taxes in order to meet future financial obligations. Roth 401-k withdrawals non-taxability will help these individuals.

What is the marketing angle?

Roth 401-k Plans will be of particular interest to highly compensated individuals. To be specific, joint filers with AGI of \$160,000 annually and single filers with AGI of \$110,000 annually, cannot contribute to Roth IRAs because of their income. As a result, Roth 401-k will be their only access to a plan with tax-free income at retirement. The Roth 401-k has no income restrictions so these individuals will be a captive audience. Any employee can participate in a Roth 401-k if the employer provides the option.

What is the danger?

The Roth 401-k was created with the Economic Growth and Tax Reconciliation Act of 2001, which was passed with a “sunset provision.” If Congress does not take action, it will expire in 2010.

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