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INDIVIDUAL RETIREMENT ACCOUNTS (IRAs)  
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Recent changes in the Nation's tax laws have made Individual Retirement Accounts available to many people previously excluded. Enclosed is general information on IRAs including material explaining these recent changes and their consequences.

Additional information on this subject, primarily in periodicals and newspapers, may be found in a local library through the use of indexes such as the Readers' Guide to Periodical Literature, Public Affairs Information Service Bulletin (PAIS), and the New York Times Index.

We hope this information will be helpful.

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**Gene Snyder**



97th Congress }  
1st Session }

COMMITTEE PRINT

A GUIDE TO INDIVIDUAL RETIREMENT  
ACCOUNTS (IRA's)

AN INFORMATION PAPER

PREPARED BY THE STAFF OF THE  
SPECIAL COMMITTEE ON AGING  
UNITED STATES SENATE



DECEMBER 1981

This document has been printed for information purposes. It does not  
offer findings or recommendations by this committee

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## PREFACE

In 1981, Congress passed legislation enhancing the tax incentives for individuals to save for retirement. Under the old law, only workers not covered by a pension plan or profit-sharing plan were eligible for tax-sheltered savings under an individual retirement account (IRA). Beginning January 1, 1982, virtually everyone with earned income will be able to contribute to an IRA and build a nest egg for the future while paying less Federal income tax now.

Money put into an IRA is deducted from gross income, and the interest, dividends, and capital appreciation on the IRA contributions are tax deferred. IRA contributions and the earnings therefrom are taxed when the money is actually distributed to the individual, which may occur when the individual's tax bracket is lower because of retirement.

This consumer guide provides a general introduction to IRA's and discusses the various savings and investment vehicles available. For specific questions on tax aspects and rules, you should consult your attorney, or you can seek answers from the Internal Revenue Service by calling the toll-free number in your local directory.

The Special Committee on Aging does not endorse any particular kind of IRA. That decision has to be a personal one. But, as you go about evaluating the various investment options, this consumer guide should help you to ask the right questions and make an informed choice about whether you should set up an IRA—and how.

JOHN HEINZ,  
*Chairman.*

LAWTON CHILES,  
*Ranking Minority Member.*

## A GUIDE TO INDIVIDUAL RETIREMENT ACCOUNTS (IRA's)

### HOW DOES AN IRA WORK?

Because the individual retirement account is a new opportunity for so many people, numerous questions have been asked about how an IRA actually works. The following are some of the most commonly asked questions:

#### ELIGIBILITY

*Question.* Who is eligible to set up an IRA?

*Answer.* Any person who earns compensation.

*Question.* How much money may I invest in an IRA each year?

*Answer.* A maximum of \$2,000 or 100 percent of your taxable compensation for the year, whichever is less.

*Question.* Is this more than was permitted under the old law?

*Answer.* Yes. Previously, the maximum was \$1,500 or 15 percent of your compensation for the year, whichever was less.

*Question.* What if both a husband and wife are wage earners?

*Answer.* Each may open an IRA and each may contribute each year up to \$2,000 or 100 percent of their own compensation for the year, whichever is less. This could total \$4,000.

*Question.* What kind of compensation qualifies?

*Answer.* Compensation may be wages, salaries, tips, professional fees, bonuses, and other amounts earned for providing personal services. Commissions and net income from self-employment also are compensation. If you are an active partner, your share of partnership earned income is compensation. However, unearned income, such as rental income, interest income and dividend income, is *not* compensation.

*Question.* What is the rule if a spouse is not a wage earner?

*Answer.* The working spouse can contribute to an account for the benefit of the nonworking spouse. This IRA belongs to the nonworking spouse. The total combined amount that may be contributed each year to the wage earner's own account and to the nonworking spouse's account is \$2,250 or 100 percent of the working spouse's compensation for the year, whichever is less. A couple can divide the contributions between their accounts as they choose, but no more than \$2,000 can be contributed to the account of either one.

*Question.* How is a divorced spouse affected?

*Answer.* A divorced person may contribute to an IRA set up for his or her benefit by a former spouse. Alimony or separate maintenance may be considered compensation that qualifies for investment in an IRA if the account was set up at least 5 years before the year of the divorce or legal separation, and the ex-spouse contributed to the account in at least 3 of the 5 years before the year of the divorce or legal separation.

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*Question.* Is there a lower or upper income limit for IRA eligibility?  
*Answer.* No.

*Question.* Is there a limit on the amount of time a person must work each year to qualify for an IRA?  
*Answer.* No.

*Question.* Are part-time workers eligible?  
*Answer.* Yes.

#### MAKING AN IRA INVESTMENT

*Question.* Do I have to put \$2,000 in my IRA every year to keep it alive?

*Answer.* No. There is no minimum contribution requirement.

*Question.* May I stagger my investment over the year?

*Answer.* Yes. Or the entire amount may be invested at one time. Contributions to an IRA must be in the form of cash, check, or money order.

*Question.* What is the cutoff date for contributions to the IRA each year?

*Answer.* Contributions may be made through the due date for your income tax return, including extensions. For most people that date is April 15 of the year following the year when the income was earned.

*Question.* When is the last date each year when I may set up an IRA?  
*Answer.* The due date for filing your tax return, with extensions.

*Question.* Where may IRA money be invested?

*Answer.* IRA money may be invested in such things as passbook savings accounts, certificates of deposit, annuities, mutual funds (including money market funds), individual stocks and bonds, and certain kinds of real estate, such as limited real estate investment partnerships.

*Question.* Are any investments forbidden?

*Answer.* Yes. Assets used to acquire a collectible are treated as immediate distributions from the account and are taxed accordingly. They may also be subject to penalties for premature distribution. Collectibles include works of art, antiques, metals, stamps, coins, and alcoholic beverages. Money invested in life insurance contracts generally does not qualify for an IRA contribution. (Annuities do qualify.)

*Question.* Is there any limit on the number of IRA's a person may have?

*Answer.* No. But only a combined total of no more than 100 percent of compensation or \$2,000, whichever is less, may be invested each year, no matter how many IRA's are set up.

*Question.* Is there a penalty for putting more than the deductible limit into an IRA in any one year?

*Answer.* Yes. An excise tax of 6 percent is levied on any amount contributed beyond the deductible amount—unless the excess and any earnings on the excess are taken out before the due date for filing an income tax return for the year.

#### MOVING AN IRA

*Question.* May I move my IRA account?

*Answer.* Yes, you may withdraw part or all of the assets from one IRA and invest them in another IRA, tax free. This is known as a "rollover."

*Question.* When must this investment be made?

*Answer.* By the 60th day after the day you receive the money from your IRA.

*Question.* How often may I do this?

*Answer.* You must wait at least 12 months between rollovers.

*Question.* Is there any way I may move my IRA from one institution to another more than once a year?

*Answer.* Yes. If the money does not pass through your hands but is handled exclusively by the institutions involved, the transaction is not considered a "rollover" and the 1-year waiting period does not apply.

#### AGE LIMITS AND WITHDRAWALS

*Question.* At what age may I open an IRA?

*Answer.* There is no minimum age. You may not, however, deduct payments you make to an IRA if you will be 70½ before the end of the year.

*Question.* When may I withdraw money from my IRA?

*Answer.* Normally, you may start to withdraw your money at age 59½. (Early withdrawals are permitted upon disability or death.)

*Question.* Must my money be withdrawn by a certain age?

*Answer.* You must begin to receive payments from your account before the end of the year in which you become 70½, whether you are retired or not. You may not invest any money after you reach 70½. There is a heavy penalty for failing to make proper distribution of the money. Work closely on this with the institution where your IRA is set up.

*Question.* How is the money in my IRA paid out to me?

*Answer.* The money can be paid out in various ways. You may take the entire amount in a single payment between 59½ and the end of the year during which you reach 70½. Or you may elect to receive the money in regular payments over a fixed period of time that is not greater than the life expectancy or the combined life expectancy of you and your spouse. Or you may choose an annuity that would make regular payments for life or the combined lives of you and your spouse. Payments must begin by the end of the tax year during which you become 70½.

#### FEDERAL INCOME TAX ASPECTS

*Question.* Do I pay any taxes on the money I put into an IRA each year?

*Answer.* No. That amount—the lesser of \$2,000 or 100 percent of taxable compensation for the year—is taken off the top of your income and is not taxed until it is distributed to you.

*Question.* Is interest or other money earned by my IRA taxed each year?

*Answer.* Money is not taxed as it accumulates in your account. There may be a few special exceptions to this.

*Question.* When is my IRA taxed?

*Answer.* When you withdraw money from your IRA, it is taxed as ordinary income, unless you "roll it over," tax free, as described above. There is a tax penalty if you withdraw money before you are age 59½. A penalty-free withdrawal can be made upon disability or death.

*Question.* What is the penalty for withdrawing my money early?

*Answer.* The amount withdrawn will be taxed as ordinary income and a 10 percent additional tax will be charged on the amount withdrawn. The additional tax is nondeductible. This penalty does not apply to an early withdrawal that is "rolled over," tax-free.

*Question.* Does my IRA become part of my estate after I die?

*Answer.* The remaining amount in your IRA is not subject to Federal estate taxes if it is paid to your beneficiary during his or her lifetime or during a period of at least 36 months. However, a lump-sum payment to your beneficiary is included as part of your estate for Federal tax purposes.

*Question.* How about gift taxes?

*Answer.* A distribution payable to a beneficiary will not be subject to Federal gift taxes.

*Question.* Where can I get more information on IRA's?

*Answer.* No matter where you live there will be a tax information number in your telephone book. Look for it under United States Government, Internal Revenue Service. Call that number and ask for Publication 590, Tax Information on Individual Retirement Arrangements.

#### WHAT AN IRA CAN PRODUCE FOR YOU

What can an IRA do for you?

Take this example, developed by a financial organization:

You are permitted a maximum investment of \$2,000 a year in an IRA.

After 20 years, you would have \$161,397 if you invested all \$2,000 on January 1 every year at 12 percent simple interest, compounded over 20 years.

After 40 years, the same investment would produce \$1,718,285 and would make you a millionaire.

But let's keep things in perspective. You would still have a real nest egg. But allowing, say, for inflation of 5 percent a year, 40 years from now \$1,718,285 would buy goods worth approximately \$244,110 in 1981 dollars.

#### IRA OPTIONS

The simplest way to invest your IRA dollars is in a passbook savings account.

But, financial institutions are also offering other IRA investments with higher returns than the passbook savings rate.

Banks, credit unions, savings and loan associations, insurance companies, mutual funds, and investment brokers all are courting the IRA customer.

Here is a rundown on options private financial institutions are making available.

#### BANKS

Banks are offering a variety of options on IRA's that are patterned after conventional certificates of deposit but are far more flexible.

Even within the same bank more than one option may be available. Conventional certificates of deposit require sizable initial payments.

But an IRA account can be opened with a modest amount, perhaps \$100. After that you can deposit as much as you like, whenever you like, depending on the legal limit per year. You can even stop paying and your account will remain active. Generally speaking, banks won't charge maintenance costs.

The different options in IRA's will revolve around the kind of interest being offered, the amount of interest, and the length of time of the certificate.

Some IRA's will have variable, or floating, interest rates. Others will have fixed interest rates.

Both rates generally will take as their guide the rates of U.S. Government securities and other investments. This does not mean the IRA necessarily will be paying the same amount as the securities. It could be paying more. But the variable, or floating rate, on the IRA would fluctuate along with the security's fluctuations. Interest on your account would be adjusted regularly.

The fixed rate will stay the same throughout the timespan of the certificate, when new terms would be set.

Although IRA certificates will have time limits of at least 18 months, some banks will renew IRA's with variable interest rates automatically if the customer wishes.

Your IRA probably won't have the same interest rate throughout its lifetime. When your certificate matures you can move your account elsewhere if you are dissatisfied with the new terms proposed. But the bank may charge a penalty if you move the money before the certificate's maturity.

Accounts in the vast majority of commercial and mutual savings banks are federally insured up to \$100,000. Others are not, but they may be insured under your home State.

#### CREDIT UNIONS

Almost all credit unions will be offering IRA's. They expect to pay interest that is competitive with other financial institutions.

Credit unions are chartered by the Federal Government or by the States.

Every Federal credit union is free to decide what kind of IRA it will have, including the interest it will pay. State-chartered credit unions also will develop their own plans, although some States have interest ceilings.

Credit unions will design IRA's keyed to their size and nature. Interest will be set by the board of directors of the credit union. Some IRA's will have no time limit. Others may offer savings certificates with a time limit and would charge a penalty for premature withdrawal.

Convenience is one of the assets of a credit union, and many credit unions will maximize convenience by offering payroll deductions for their IRA's.

The initial deposit required generally would be very low, such as \$25 or less. For those not taking advantage of payroll deduction, additional deposits generally could be made at any time and in any amount, as long as they don't exceed the legal limit each year. For the most part, no maintenance fees will be charged.

Accounts in Federal credit unions are federally insured up to \$100,000. Some State-chartered institutions also are federally insured. Others may be insured by the State for a comparable amount.

#### SAVINGS AND LOAN ASSOCIATIONS

Savings and loan associations will be offering a range of options which are variations of conventional savings certificates that are tailored especially for IRA's. Some savings and loans will offer more than one option.

IRA's at savings and loans will differ in the kind of interest offered, in the rate of interest, and in the length of time the savings certificate runs.

Interest rates generally will be pegged to the rates of U.S. Government securities or other investments. Most savings and loan associations will choose an interest rate that the customer can understand easily, such as the rates on Government securities that are published regularly in newspapers.

This does not mean the interest rate must be the same as the rate on the Government security. The savings and loan could be offering higher or lower interest.

Some IRA's will have a variable, or floating, interest rate that will rise or fall when the rate changes on the security to which it is pegged. Adjustments in the interest rate would be made regularly.

Other IRA's will have fixed interest rates that will remain the same during the time period of the savings certificate, which could be for 18 months or could run for several years.

Your IRA plan probably won't have the same interest rate throughout its lifetime. When your savings certificate matures you are free to move your IRA elsewhere if you are not satisfied with the new terms proposed. However, if you take your money out before the certificate's maturity, the savings and loan association may charge a penalty.

Savings and loans generally require a modest deposit—for example, as low as \$10—when you open your account. After that you may deposit what you like, when you like, as long as you don't exceed the legal limit each year. You can even stop paying and your account will remain active. Maintenance generally will be free.

Accounts in the vast majority of savings and loans are federally insured up to \$100,000. Others are not, but they may be insured under your home State.

#### INSURANCE COMPANIES

An IRA set up with an insurance company is an annuity. An annuity guarantees you an income as long as you live. It is the only IRA that can provide this guarantee.

Insurance companies will tell you in the beginning what the fixed minimum rate of interest will be on your money through the years. The advantage is that guaranteed interest is not subject to market fluctuations. This interest rate could be spelled out in stages in your policy. For example, the guaranteed rate could be relatively high in the first or early years, and then lower for succeeding years.

On paper, the guaranteed rate of insurance companies has been considerably lower in recent years than rates offered by other financial institutions. In reality, insurance companies have been paying interest which is more than the guaranteed rate and is competitive with other institutions. The only *guaranteed* rate, however, is the one spelled out in the policy.

IRA's have flexible premiums. This means you can put as much as you like in your IRA at any time, as long as you don't exceed the maximum set by law each year. You can even stop paying and your policy still will be in force. Some companies will accept \$50 or less as an opening amount.

Some companies are tailoring policies especially for IRA's by offering fixed interest annuities that have no "front loads," which are sales costs. Your entire investment will be earning money for you. But you can expect to pay sizable penalties if you withdraw your money prematurely, particularly in the early years of the policy. This is called "backload."

Maintenance fees for IRA's will run around \$20 or \$25 a year.

Your fixed annuity also guarantees a rate upon which payments to you will be based. You can never get less, but you could get more.

Some insurance companies will also offer IRA's that do not have guaranteed interest. They are called variable annuities. The value of the annuity fluctuates, depending on market conditions. They generally will have sales costs.

Money in your annuity will not be federally insured, but State agencies that regulate insurance companies emphasize safety and diversity in investments.

#### MUTUAL FUNDS

When you put your money in a mutual fund you are buying shares in a pool of money that is invested in securities chosen by professional money managers.

The most famous type of mutual fund is the money market fund, where money is invested in short-term securities and your rate of return varies daily.

Other mutual funds invest in stocks and bonds.

Every mutual fund is made up of a group of securities. There are hundreds of mutual funds, designed to meet different objectives of investors.

Mutual funds do not guarantee a specific rate of return on your investment. Some funds have far outstripped increases in the Consumer Price Index. But it also is possible to lose money in a mutual fund investment.

Mutual funds are known as load and no-load funds. The "load," or charge, is a sales commission paid to a broker or sales agent for advice and services. The sales charge usually is around 8.5 percent of the cost of every purchase of shares in the fund.



Generally speaking, shares in no-load funds are not purchased from a broker. Money market funds, which are no-load funds, are an exception to this.

There is virtually no difference in the investments of no-load and load funds. You must be given a prospectus spelling out the objectives and terms of each fund.

You can move your IRA from one mutual fund to another as your own investment objectives change. Generally, there are no charge when you sell fund shares.

Some funds may require that you invest at least a minimum amount—perhaps \$100—every time you buy shares. Others require no minimum.

Each year, there will be a management fee that is usually around 1 percent of the value of your shares. Money market funds generally charge half this amount. Many funds also charge a maintenance fee for your IRA of about \$10 a year.

Mutual funds seek to achieve investment growth, safety, and stability through diversified investment, but you should carefully check the sales prospectus to evaluate how much risk is involved. In a mutual fund, your money is not insured against loss due to normal market action.

#### INVESTMENT BROKERS

Brokers offer the widest range of IRA choices.

For example, brokers at investment firms can set up IRA's in mutual funds.

They can arrange to put your IRA in a limited partnership built around income-producing real estate.

They can help you select an annuity.

If you want to manage your own investments, they can help you arrange for a self-directed individual retirement trust that will qualify as an IRA.

Investing in securities, however, carries the risk of loss as well as gain.

You may find that some IRA investments made through a broker will have higher costs associated with them than other IRA's have. A broker will charge about 8.5 percent of the cost of every purchase of shares in a mutual fund. Even in a self-directed IRA, you will pay a broker's commission when you buy or sell stock. There also will be some costs for establishing the plan and administering it.

In some cases, the kind of investment you select will require commitment to a specific investment, up to the limit of the IRA. For example, you could be required to invest \$2,000 at one time in a limited real estate partnership.

Investments made through a brokerage firm are not insured against loss due to normal market action. However, client accounts are insured up to \$500,000 against loss due to failure of the firm.

#### POINTS TO CHECK

When it comes time to shop for your IRA, remember this: It's a buyer's market. Financial institutions are competing aggressively for your money.

First of all, find out if your employer is accepting deductible, voluntary IRA-type contributions to a pension plan.

Also, find out if your employer has agreed to a payroll deduction plan for IRA's that is not related to a pension plan. The money would be invested by a financial institution and you could select the IRA you want. The range and nature of investment options might be greater than if you went to the financial institution as an individual.

Still, you may prefer to locate an IRA on your own.

Be sure to shop around. Ask to talk to the IRA specialist at various financial institutions. They all have one.

Make sure the institution has been approved for IRA's. Banks, savings and loan associations, and federally insured credit unions are eligible to act as trustees automatically. Other institutions must be certified by the Internal Revenue Service. Ask the institution for written proof of certification.

Consider what you want an IRA to do for you and explore in those terms. Assess your temperament, age, and retirement income needs. Weigh the relative safety of your investment options. Generally speaking, the closer you are to retirement, the more conservative your investment choice may be, particularly if you will be depending heavily on IRA dollars. You might also consider opening IRA's in different financial institutions to diversify your retirement investments.

Make certain to get the disclosure statement required by law. The trustee must give you an explanation of all the income tax consequences of opening and maintaining an IRA account.

If the rate of return on the IRA is guaranteed or can be reasonably projected, this disclosure statement must give you a projection of the growth of the program at the end of *each* of the first 5 years of the contract and at age 60, 65, and 70. Among other things, the statement also must give startup and administrative costs.

If the investments are made in mutual funds or on the open market, you must instead be informed of what sales and administrative charges will be made against your contributions and how annual earnings are figured.

Ask about the minimum amount required by an institution to open an IRA.

Make a point of understanding the kind of interest, or other return, that is being offered. Ask how interest will be calculated, too. It makes a difference in the dollars coming to you.

Interest rates and fees will vary from institution to institution and from locality to locality. Understand, also, that in many cases, interest rates will not remain the same during the life of your IRA.

Keep in mind that you can move your IRA without incurring a tax penalty, but the institution you are leaving may charge a penalty for early withdrawal.

# Best Ways to Cash In On IRA Tax Breaks

**New savings plans can help you prepare for retirement. But there are rules to follow and choices to make. Here's what you need to know.**

Working Americans who are willing to start socking away cash for retirement are now getting a big new helping hand from Uncle Sam.

Effective January 1, tax breaks reward individuals who put up to \$2,000 a year into a special savings plan—known as an individual retirement account—to build a nest egg for the future. Money put into an IRA can be invested in any number of ways—from simply opening a savings account at a bank to trading in stocks and other securities. You can have a professional manage the money in your account or you can do it yourself.

As a result, a whirlwind of bidding is under way by firms seeking to handle the flood of investment money. Banks, savings and loan associations, mutual funds, credit unions, insurance companies and stockbrokers are all offering IRA investment plans. Some companies are setting up payroll-deduction plans for IRA contributions.

Financial institutions are "fighting tooth and nail" for this money, says William Donoghue, publisher of a newsletter on money-market mutual funds.

The American Bankers Association says more than 50 billion dollars a year could flow into IRA programs, although much of this money will come from cash earmarked anyway for investments and savings.

## Tax Benefits

What makes IRA's attractive are two big tax benefits—

- The money that you contribute to an IRA is deductible from your income before calculating how much federal income tax you owe, even if you don't itemize any other deductions.

For example, a person who would otherwise have annual taxable income of \$28,000 would

only have \$26,000 after contributing \$2,000 to an IRA. For a married couple filing a joint return, that reduction means a 1982 tax saving of \$580. In effect, it costs this couple only \$1,420 to make a \$2,000 investment. The savings are bigger for people in higher tax brackets, smaller for people in lower tax brackets.

- Interest and other earnings on the IRA investment, including capital gains, accumulate without being immediately taxed. That lets the value of your IRA snowball since the balance upon which you can earn investment income isn't reduced by a tax bite.

## Who's Eligible

Until this year, IRA's had been limited to people who weren't covered by an employer-sponsored retirement plan. Last year's big tax-reduction bill changed that. Starting in 1982, anyone who gets compensation from employment, including fees for professional services or income from part-time work, can set up an IRA, even if also covered by an employer's retirement plan.

An individual holding a job can put up to \$2,000 a year into an IRA. Open a separate account for a nonworking spouse who doesn't receive any pay during the year, and you can put away a combined total of \$2,250—split in any ratio, but no more than \$2,000 to either account. If you and your spouse both work, you can each invest up to

\$2,000. If you run a business, it may pay to hire your spouse part time to allow both of you to have IRA's.

The main limit on IRA contributions is that you can't contribute more than what you receive in on-the-job compensation. That's of special interest to part-time workers. Nor can you make contributions if your only income is from interest, dividends or other non-employment sources.

As long as you don't exceed the yearly ceiling on contributions, there is no limit to the number of individual IRA's you can have. Moreover, you are not locked into an IRA. Within limits, you can close old IRA's and open new ones, or sometimes switch the type of investment within an IRA. The tax rules don't require you to put money in every year, and the payments you make don't have to be in a lump sum. Some sellers of IRA investments, however, may require a minimum deposit.

Self-employed persons can set up IRA's, too, even if they also have IRA-like Keogh retirement plans.

## Returns You Can Get

The key to benefiting from an IRA is to "start early and contribute consistently," says Gary Strum, a vice president at E. F. Hutton & Company, the investment firm.

For example, a person who is now 40 years old and pays in \$2,000 a year to an IRA that earns 8 percent a year compounded quarterly would accumu-



## What an IRA Could Earn...

Here's what could happen to an individual retirement account in which \$2,000 was invested each year—

Age When Started	Total Deposit by Age 65	Dollars Accumulated at 8% Interest	Dollars Accumulated at 12% Interest
30	\$70,000	\$393,853	\$1,106,452
35	\$60,000	\$256,456	\$ 604,611
40	\$50,000	\$163,999	\$ 326,754
45	\$40,000	\$101,778	\$ 172,911
50	\$30,000	\$ 59,905	\$ 87,732
55	\$20,000	\$ 31,726	\$ 40,570
60	\$10,000	\$ 12,762	\$ 14,458

Double the amounts for a working couple who contribute \$4,000 a year.

Note: Figures assume deposits made at start of period, with interest compounded quarterly.

## Vs. Inflation's Erosion

Annual Rate of Inflation	Value of Today's \$100,000 in		
	5 Years	15 Years	25 Years
6%	\$74,726	\$41,727	\$23,300
8%	\$68,058	\$31,524	\$14,602
10%	\$62,092	\$23,939	\$ 9,230
12%	\$56,743	\$18,270	\$ 5,882
14%	\$51,937	\$14,010	\$ 3,779

USNEWS tables

**National Permanent's IRA PLUS PLAN**  
No Commissions, No Fees

**We've got your IRANSWER.**

**IRA YOU QUALIFY!**

**All IRAs may look the same. Until you retire.**

**IRAS FOR EVERYONE IN 1982**

Financial firms are waging an advertising war to woo customers for individual retirement accounts. At stake are billions of dollars in new savings.

late \$164,000 by the time he or she reaches 65. If the IRA earns 12 percent a year, the balance will reach almost \$327,000; start at age 30, and by age 65 you can have more than 1 million dollars stockpiled, even though your contributions totaled only \$70,000. One New York S&L advertises: "Retire a millionaire for just \$166.66 a month."

But don't let the gargantuan figures blind you. Behind the assumption that you can earn 12 percent a year, for instance, is an assumption that high inflation will continue. If that is so, by the time you retire, 1 million dollars won't be worth nearly as much as it is today.

In addition, an IRA only defers tax; it doesn't exempt you from it. When you start withdrawing funds, you will be taxed on all you take out—at regular income-tax rates. Moreover, no special favor will be given to IRA earnings from long-term capital gains—such as the sale of stock held longer than a year. Capital gains will be taxed the same as other income, rather than at the lower rate that normally applies.

Nevertheless, financial advisers say IRA's still shape up as a good buy. They also note that the tax bite may be eased at retirement when you presumably will be in a relatively low tax bracket because you won't be working.

In addition, advisers say that people should start IRA's because Social Security and private pensions cannot be counted on to provide all the cash needed for retirement.

Despite the hoopla, there's no need to rush into an IRA. Though opening an IRA early this year will get you a fast start on earning tax-deferred income, you can wait until you file your 1982 tax return in 1983 to open an IRA or make a contribution to one, and still get a 1982 tax deduction.

### Where to Invest

Many people are likely to open accounts at banks or savings and loans, which have garnered the bulk of IRA's in the past. One big drawing card: Federal insurance for up to \$100,000. After your IRA tops that amount, you can open more at other banks and S&L's to stay fully insured.

IRA funds can be put into any bank or S&L account, but most heavily promoted are certificates of deposit specifically aimed at IRA funds. They have a maturity of 18 months or more and can pay any rate of interest an institution wants, though the rate is generally linked to that paid on government and other money-market securities. Some banks in December were offering up to about 14 percent a year on such CD's. Many institutions offer a choice: A certificate with a fixed rate or one with a rate that varies with money-market yields. Credit unions also may offer special IRA savings certificates.

Mutual funds hope to pull in a large share of IRA accounts because of the flexibility and variety of investment that funds allow. Some investors are expected to start off with money-market funds, possibly switching later to funds investing in common stocks. Dreyfus Service Corporation, as one example, allows its IRA clients to switch without charge between six mutual funds it manages. Included are bond, stock and money-market funds.

Insurance firms offer several plans—including annuities that guarantee a minimum income level for life after you retire.

The greatest flexibility is offered by accounts you can manage yourself through a stockbroker. Merrill Lynch lists 19 investments open to its IRA clients, including stocks, bonds, U.S. se-

curities, mutual funds, options and real-estate partnerships. Note: Deposits to an IRA must be in cash. You can't contribute assets, such as stocks, you already own.

Also available for investment are special U.S. individual retirement bonds, available from Federal Reserve banks and the Treasury. They yield a relatively modest 9 percent a year.

Specifically prohibited for new IRA investments are gold, art, antiques, diamonds, coins and other so-called collectibles. An alternative is to invest indirectly in such assets—shares in a gold-mining firm, for example.

Experts suggest you stay away from tax-exempt securities, such as municipal bonds. The reason: The interest on such securities are less than on other investments and yet don't escape tax in an IRA—they are taxed when withdrawn.

More controversial is the question of investing in stocks. Some analysts look askance at buying securities for long-term price appreciation because shares held in an IRA don't get favorable long-term capital-gains treatment. Instead, these analysts suggest buying stocks that pay big dividends, or high-yielding debt issues such as bonds and government securities, to benefit from the tax deferral in an IRA. Others, however, say that even though you give up capital-gains benefits, stocks may still be the best bet for long-term growth to outpace inflation.

Many employers are allowing payroll deductions to IRA's; this offers convenience and often lower costs. NCR Corporation in Dayton, Ohio, for one, gives employees a choice. They can funnel their money to NCR's credit union, a mutual fund that is managed by T. Rowe Price Associates, or a program run by Connecticut General Life Insurance Company for investing in long-term securities.

The new law also allows employers to accept IRA-style deposits to a firm's own pension plan, although that approach appears to be less popular.

### Withdrawals

Though IRA's are billed as a way to save for retirement, your age rather than job status determines when you can withdraw money. You can take cash out without penalty, gradually or all at once, as early as age 59½, and the balance still accumulates tax deferred.

Unless you become disabled, withdrawals before 59½ are subject to a tax penalty of 10 percent of the amount withdrawn, in addition to your being hit by income tax. The same age limits on withdrawals apply to a spouse for whom you've opened an IRA. There's no early withdrawal penalty if you die,

in which case your IRA assets can be passed on to heirs.

Note: You can't get around the early-withdrawal penalty by borrowing from an IRA or using its assets as collateral for a loan. Do that and you are subject to penalty and tax as if the amount were an early withdrawal.

Nevertheless, advisers say that people shouldn't let the withdrawal penalty scare them. That's because the tax breaks are so large that in some cases in future years you may come out ahead even if you must incur the penalty.

You must start withdrawing from an IRA after you reach 70½. At that point, the withdrawals must be at a rate fast enough to deplete the IRA over either your life expectancy or the joint expectancy of you and your spouse. You can make contributions to an IRA up to the year in which you reach 70½.

But even people under 59½ can take out IRA funds temporarily without incurring a penalty or tax. Once a year you can close an IRA and hold the funds for up to 60 days before rolling them over into a new account to avoid tax or the 10 percent penalty. You can use the funds as a short-term loan or invest them to get current income.

If you want to switch an IRA more than once a year, the institution holding your account must transfer it to the new institution, thus keeping the funds out of your hands and preventing you from being hit with tax or penalty. Note: Though you avoid tax penalties in such a transfer, you may run into extra charges levied by the institution in which you have your IRA—an early-withdrawal penalty on a savings certificate or a redemption fee on an insurance annuity, for example.

### **The Cost**

When opening an IRA, there are often initial charges to pay, as well as an annual fee, sometimes based on the value of the account. But the levies are generally small. Banks and S&L's usually charge nothing to open an IRA and \$10 or less a year to maintain it. Many mutual funds charge \$5 to \$10 to open an IRA and less than \$10 a year to keep it up. Self-directed accounts at stockbrokers may cost up to about \$30 to open, with a maintenance fee of about \$25 or higher depending on the account's size and type. You also pay commissions on the purchase of stocks and some mutual-fund shares and insurance annuities.

The best advice: Shop around, don't be misled by fancy sales pitches and be wary of promises of high future yields that may not be met. □

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By LEONARD WIENER

U.S. NEWS & WORLD REPORT, Jan 11, 1982

## Your Money Matters

# To Decide Where to Put Your IRA Dollars, Look at Risks, Management and All the Fees

By JILL BETTNER

Staff Reporter of THE WALL STREET JOURNAL

For millions of people, the question isn't whether to open an individual retirement account (IRA) after Jan. 1, but where.

Financial institutions, brokerage firms, credit unions, insurance companies and mutual funds are all competing for your business, as you have undoubtedly noticed from the barrage of advertising in recent weeks.

Whatever investment you choose, any amount that you contribute to your IRA will be tax-deductible, up to \$2,000 a year, or a total of \$2,250 for yourself and a nonworking spouse. The earnings can be left to accumulate tax-free until you reach at least age 59½.

Deciding how to invest depends on the risk you will accept in return for a possibly higher tax-free yield, whether you want to control your IRA yourself or have it professionally managed, and how much you want to pay in assorted fees (see accompanying table).

No matter where you put your IRA dollars, if you dip into the account before age 59½, you will pay a penalty tax of 10% on the amount withdrawn. And, the money you take out will be taxed as ordinary income.

For instance, if you accumulate \$10,000 in an IRA and decide to take out \$2,000 before you reach the magic age, you will pay a penalty tax of \$200. The other \$8,000 will remain sheltered. If, however, the \$10,000 was invested in a bank certificate of deposit or an insurance annuity, you could also pay other penalties for getting at the money early.

Still, the tax penalties for early withdrawals from an IRA aren't prohibitive. After a few years, they can effectively be paid out of tax-free interest.

(Note: While annual contributions to the new universal IRA are a write-off on your federal tax return starting in 1982, many states, including New Jersey and California, haven't amended their laws to make the contributions deductible from state income taxes. Most state legislatures, however, are expected to act in time for claiming the full deductions for 1982.)

Any fees for setting up or maintaining an IRA are also deductible from federal taxes, whether you choose to pay them out of your annual contributions or separately. Here is a sample of the types of investments available from various institutions:

**Banks, Thrift Institutions and Credit Unions.** The options include certificates of deposit with a choice of maturities, as well as regular passbook savings accounts. Their fees are the lowest, and IRAs are federally insured, up to \$100,000.

New are 18-month certificates, permitted only for IRAs and Keoghs, which are retirement plans for the self-employed. These "wild-card" CDs can carry any interest rate that a financial institution chooses to pay. Most banks and savings and loans are currently advertising rates of between 14% and 15% on either fixed- or variable-rate 18-month certificates. Minimum deposits can be as low as \$1. Credit unions can vary the term, as well as the rate, on any certificate they decide to offer.

If you have an existing IRA or Keogh, and you are stuck with an old, low-interest savings certificate that hasn't matured, you can avoid an early-withdrawal penalty and still start earning more on contributions toward your retirement savings from now on.

A financial institution can assess an early-withdrawal penalty, which requires you to forfeit at least the last six months' interest, only if you invade the certificate's principal. But you can withdraw the accumulated interest without penalty any time. (The same is true of any kind of savings certificate.)

Use the interest you have piled up to open a higher-paying IRA or Keogh, and direct that the future interest on your old certificate also be paid to the new plan. It is called "bleeding" an account, and although banks hate people who do it, few of them charge any fee for such automatic interest transfers.

**Brokerage Firms.** The big brokerage houses offer the most variety of investments, although you will pay more in fees for your IRA than you will at financial institutions. And brokerage retirement accounts aren't covered by federal deposit insurance.

Basically, there are two ways to go. A self-directed IRA lets you buy and sell stocks and bonds as you like, or control investments in such things as real estate, oil and gas or equipment leasing. At Paine Webber Jackson & Curtis Inc., investors can buy mortgage securities insured by the Government National Mortgage Association (Ginnie Mae). The fees, which are typical of those the firm charges for all of its self-directed accounts, are \$25 to open an IRA, brokerage commissions of \$30 per \$1,000 invested, plus a \$25 annual maintenance, or custodial, fee.

Merrill Lynch will charge \$30 to open any kind of self-directed IRA, plus brokerage commissions. The annual maintenance fee will be the greater of \$50, or two-tenths of 1% of the assets in the account as of Dec. 31 each year. Bache Halsey Stuart Shields Inc. will have fees of \$25 and a minimum annual fee of \$35.

The lower-cost route at a brokerage firm is to invest in any of the professionally managed mutual-fund packages the firm sells. Typically, the packages include a money-market fund and several types of stock funds and bond funds. Also available are funds that combine stocks and options. There is usually a fee of about \$5 to switch out of one fund and into another.

Merrill Lynch will charge \$15 to set up a mutual-fund account, plus an annual custodial fee of \$20. Dean Witter Reynolds Inc. will charge \$20 and \$20, respectively.

**"No-Load" Mutual Fund "Families."** Firms like the Fidelity Group, the Dreyfus Service Corporation, T. Rowe Price and the Vanguard Group offer IRA investors several professionally managed funds without sales charges.

At most companies there won't be a charge for setting up the account or for switching between funds. Annual management fees typically will run \$10 or less.

All of the big companies are also aggressively marketing their funds for payroll-deduction IRAs. If your employer offers such a plan, participating in it could cost you less than buying the funds directly.

**Insurance Companies.** The products are called Individual Retirement Annuities. Their biggest selling point is that they are guaranteed to provide a certain amount of income each year after you retire. The payout, per \$1,000 you invest, is based on average life expectancies, as well as the value of the investments purchased with premiums.

There are two main types of insurance IRAs. Prudential, for instance, will offer a "front-loaded" annuity that will carry a sales charge of 8.75%, which comes off the top of each \$1,000 you put in over the years. The initial interest rate, which will be adjusted annually, will be 13.75%. The annual maintenance charge will be \$8 on the first

payment, \$1 on any subsequent payments. There won't be any penalties to withdraw part of your funds.

Prudential will also have a "back-loaded" annuity that will pay 13% to start. There aren't any sales charges on this type of contract, but there is a penalty of 7% if you withdraw any money in the first year. That penalty scales down gradually until it disappears entirely in the eleventh year. The annual maintenance fee is \$25, starting in the second year.

Several insurance companies will also offer variable-rate annuities that invest in mutual funds. Northwestern Mutual Life's plan will give buyers the choice of a money-market fund, stock fund or NML I, a fund that will move in and out of various investments "as market conditions warrant," a company spokesman says. This is another back-loaded plan, which will charge a penalty of 8% of principal for withdrawals made in the first five years. The annual maintenance fee is \$30.

Shopping for an IRA				
	Investment Choices	How Much You Will Pay		
		Initial Charges to Open Account	Annual Maintenance or Management Fees	Early Withdrawal Penalties
<b>Banks and Thrift Institutions</b>	Certificates of deposit	Usually none	\$10 or less	Minimum six months interest
	Savings accounts			None
<b>Self-Directed Brokerage Firms</b> "Load" Funds	Stocks, bonds, Ginnie Maes, real estate, oil and gas	None to \$30	\$25-\$50, plus any brokerage commissions	None
	Money-market, stocks, bonds, stocks and options	8 1/4% of investment	\$2-\$9, \$5 to switch funds	None
<b>Credit Unions</b>	Certificates of deposit	None	Usually none	Minimum six months interest
	Savings accounts			None
<b>"Front-Load" Insurance Cos.</b> "Back-Load"	Fixed-premium annuities	8 1/4% of investment	About \$8-\$10	Usually none
	Variable-premium annuities	None	About \$25-\$30	7%-8% first year
<b>"No-Load" Mutual Fund "Families"</b>	Money-market, stocks, bonds, stocks and options	\$5 or less	\$10 or less Free switching	None

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# What to look for in making an IRA kitty

By Thomas Watterson  
Business correspondent of  
The Christian Science Monitor

**Boston**  
OK, you have decided the new individual retirement accounts (IRA) are a good idea. They save on taxes. They can offer a firm savings program. You can now put aside up to \$2,000 a year, even if you are already covered by your company's retirement program.

But where should you invest your IRA money?

There are banks, savings-and-loan associations, brokerage houses, mutual funds, insurance companies, and credit unions — all putting on an advertising blitz to pull in as large a share of these accounts as they can. Much of the money going into IRAs now is probably "old" money simply being shifted from one account to another. Some is "new" savings that will help fill financial institution coffers.

The accompanying table shows the six main financial institutions that are competing for the 40 to 60 million potential IRA customers. The listed products, interest rates, and restrictions for each category are, of necessity, very general. So, wherever you shop for an IRA, here are some possibly useful questions:

- What is the interest rate? How is it calculated? How often is it compounded? Is the rate guaranteed for a specific length of time?
- What is the minimum initial investment? What is the minimum on subsequent investments?
- Are there charges to open the account? If so, is this a flat fee or is it a percentage of the deposit?
- Can I contribute to the IRA through payroll deduction?
- Are there any annual charges?
- Are there any charges to transfer money from one of your accounts to another account, as from a money fund account to a bond fund?
- What are withdrawal penalties if you want to take your money somewhere else?

The IRA accounts: who has what?

Institution	Investment choice	Interest rate (1982)	Minimum investment	Initial charges	Annual charges	Withdrawal penalties
<b>Banks</b>	Certificates: 18-month variable 18-month fixed 30-month variable 5-year fixed	11 to 15 percent	\$100 to \$1,000	None	None	6 months interest
<b>Savings-and-loans</b>	Certificates and passbooks, 18- to 30-month variable or fixed rates	7 to 14 percent	None to \$500	None	None	6 months interest
<b>Mutual funds</b>	Money market fund Growth stock fund Bond fund Income fund Growth stocks	11 to 15 percent	None to \$1,000	None, usually	\$3 to \$15	None
<b>Brokerages</b>	Self-directed mutual funds	Unknown	None to \$1,000	5% to \$25, front load	None, but some commissions	None
<b>Credit unions</b>	Share accounts	10 to 14 percent	None	None	None	None, to 3 months' interest
<b>Insurance companies</b>	Fixed annuities, mutual funds	12 to 14 percent	\$15 to \$600	None to 8.75%	None	7% drops to none

Here are a few additional points to consider:

- Your first investment decision need not be your final one. Many institutions have little or no charge for transferring or withdrawing your money. The law permits you to shift your IRA account once a year to another investment vehicle. You must make the shift within 60 days after withdrawing from the first IRA.

Federally insured depository institutions, such as banks, savings-and-loans, and credit unions, probably offer the safest IRA vehicles, particularly for people who don't want to be tending their account. The 18- to 30-month certificates offered by banks and S&Ls are paying, according to their

ads, from 12 to 15 percent interest at maturity.

- Put money into your IRA account as quickly as you can. If you can afford it, put the entire \$2,000 in now and start collecting interest immediately. The effect of compounding — especially if it is done daily — means the sooner the money goes into the IRA, the more it will earn.

- Don't get hung up on the \$2,000 figure. Many people are saying, "I can't afford to put \$2,000 a year in an IRA." They should put in what they can afford. Even if it is only \$500 (less than \$10 a week), that's \$500 that is not taxed by Uncle Sam this year and will probably be taxed at a lower rate at retirement.

# Taking a cold, hard look at the million-dollar IRA

By Francine Kiefer  
Business correspondent of  
The Christian Science Monitor

Think of it, at age 65 you could retire with a comfy individual retirement account — worth a million dollars. It's right there in print. . . just like the ads say.

The ads are hard to miss. They are put out by banks across the country, and many run full-page in daily newspapers. Their simple message is this: open an Individual Retirement Account, save \$2,000 a year, retire on a million.

Is this for real? Yes and no. Mathematically, these millionaire ads are accurate. If you pump the maximum allowed (\$2,000 if you're single, \$4,000 if you're married) into your IRA at the beginning of every year, it will reach the million mark in almost 35 years. The banks arrive at this grand total by figuring a 12 percent rate of return, compounded daily — a reasonable rate in today's economy.

But what if that 12 percent rate doesn't stick around for the next 35 years? And will \$1 million still be worth \$1 million in today's purchasing power then? And how easily can people

put \$2,000 or \$4,000 aside by the beginning of every year? None of the ads guarantee the 12 percent over the life of the IRA. At Dry Dock Savings Bank in New York, which runs full-page "millionaire" ads in the New York Times, Joseph Ludovico says the bank guarantees 12 percent interest for 18 months. Mr. Ludovico, pension services manager for the bank, says the 12 percent rate works out to nearly 13 percent because of the daily compounding.

"I feel uncomfortable about the ads," says Barnet Berin, director of program standards at William M. Mercer Inc., a major pension employer benefit firm. Berin says 12 percent is "very high" and can't be counted on to continue. "Over the long run, interest rates have been well below 12 percent," he adds. It would be much better, he suggests, "if the ads showed what would happen at low, medium, and high rates."

Interest rates make a big difference in the end sum. Let's say the IRA was figured on 8 percent instead of 12 percent, same rules still applying. What might have been a nest egg of \$2,131,620 after 40 years would come down to \$612,380, says Michael Ryan, principal and actuary at Towers, Perrin, Forster & Crosby, another pension consulting firm.

Kenneth McLennan, an economist with the Committee for Economic Development, says the "retire a millionaire" campaign is "a little optimistic." He adds: "As the prime lending rate begins to fall substantially in the next 5 years, banks simply will not make it [the \$1 million goal]."

Of course, it's debatable whether the rates will fall as Mr. McLennan predicts. But, he says, if the prime rate doesn't fall and stays where it is (around 15 percent), the 12 percent rate of return will hang on . . . and so will high inflation. And that means \$1 million will not be worth \$1 million in 1982 purchasing power a couple decades down the pike.

If we assumed a 10 percent rate of inflation over the next 25 years, \$1 million would be worth \$58,820 in today's dollars. However, "this country's democracy couldn't last through so many years of high inflation," Mercer's Mr. Berin suggests.

Mark Clark, a spokesman for the United States League of Savings Associations, says that what the "millionaire" ads do is force people to recognize that "self-managed retirement plans can result in a significant nest egg for everyone. It shows people how fast tax-free, compounded interest can accumulate." If you're in the 50 percent tax bracket, Mr. Clark says, tax-free IRA accumulation over 35 years will be nearly 10 times more than if it were taxed.

There's still the question of how many people will be able to put aside that maximum amount for their IRA every year. Many people will be opening an IRA in addition to their own employee pension plan. Barnet Berin says, "people under the social-security wage base [\$32,400] would have problems saving it." Michael Ryan thinks it will be done "by people . . . whose family expenses [mortgage, car, etc.] have subsided."

Dry Dock's Mr. Ludovico disagrees. He emphatically states that "people wanting to carve a niche for themselves will be able to do it." The incentive is in the extraordinary accumulation of interest, he exclaims.

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