Are Roth Contributions Right For You?

Many people save for retirement by contributing pre-tax money from their paychecks to a workplace retirement plan.

Pre-tax contributions are made before income taxes are applied, which can reduce current taxable income. As a result, taxes may be deferred until funds are withdrawn in retirement, when distributions are generally subject to income tax.

Traditional contributions vs. Roth contributions

Roth contributions, you use after-tax money. You pay taxes on your income now, but when you retire, qualified withdrawals and any earnings are usually tax-free.

What matters most

Choosing between these options often depends on your tax situation.

The choice between pre-tax and Roth contributions is often influenced by expectations about future tax rates. Pre-tax contributions may be more advantageous when tax rates are anticipated to be lower in retirement, whereas Roth contributions may be more favorable when tax rates are anticipated to be higher in retirement.

Since it's hard to know what future tax rates will be, some people use both options.

How the numbers can compare

The hypothetical chart below shows how paying taxes at different times can lead to different results, even if you contribute the same amount.

Each example uses the same contribution amount, but the results change depending on your current and future tax rates. Here's what the chart shows:

- Pre-tax contributions aren't taxed now, but you'll pay taxes when you take the money out in retirement.
- Roth contributions are taxed now, but qualified withdrawals in retirement are tax-free.
- If your tax rate is higher now than it will be in retirement, pre-tax contributions might leave you with more money in retirement after taxes.
- If your tax rate is lower now than it will be in retirement, Roth contributions could give you more money in retirement after taxes.

When you pay taxes can make a big difference to your results.

Whether you pay taxes now or later can change your results. Knowing how each option works can help you make better decisions.

Please consult a financial professional for guidance based on your personal situation.

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	Traditional Contributions (Pre-tax)	Roth Contributions		
	A	B	C	D
Current Tax Bracket	N/A	15%	25%	35%
Contribution Amount	$5,000	$5,000	$5,000	$5,000
Federal Taxes Paid at Time of Contribution[1]	$0	($750)	($1,250)	($1,750)
Net Contribution	$5,000	$4,250	$3,750	$3,250
Value in 20 Years[2]	$23,305	$19,809	$17,478	$15,148
Federal Taxes Paid at Retirement (25% tax bracket)[1]	($5,826)	$0	$0	$0
Net Distribution	$17,479	$19,809	$17,478	$15,148

[1] State income taxes may also apply.
[2] Assumes an annual rate of return of 8%.

Other considerations

Roth contributions can be a good choice if you want greater certainty about future taxes or plan to leave money to your beneficiaries. They offer flexibility when it comes time to take withdrawals.

A thoughtful approach

There isn't one right answer for everyone. Your income, tax situation and long-term goals all matter.

If you are unsure which approach may be appropriate, a financial professional can help you evaluate your options.

For more information, visit myplanconnection.com.