THREE THINGS YOU DIDN'T KNOW ABOUT RETIREMENT ACCOUNTS

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Retirement accounts are a cornerstone of financial planning, offering a safety net that promises financial security when it's time to step away from the workforce. While you're diligently contributing to your 401(k) or IRA for decades, you don't want to discover years later that there were opportunities you missed simply because you didn't know they existed. Retirement planning isn't just about saving; it's about understanding how to make your savings work harder for you.

There's more to these accounts than meets the eye, including some long-term growth and tax advantages that can help secure your golden years. For many Americans, especially those approaching retirement, understanding lesser-known features of these accounts can make a significant financial difference. Here, we explore three insights that might just change the way you think about your nest egg.

BORROWING FROM YOUR 401(K)

One of the most surprising features of a 401(k) is the ability to take a loan against your own retirement savings. Unlike traditional loans that come with interest payments to a bank or lender, borrowing from your 401(k) allows you to pay interest back into your own account, essentially reinvesting in your future. This can be a lifesaver in emergencies, such as covering medical expenses, consolidating high-interest debt, or funding major home repairs.

Because the interest payments go back into your account, you're essentially paying yourself rather than a financial institution. This can save you thousands of dollars in interest compared to high-rate credit cards or personal loans. To qualify for a 401(k) loan, you must meet certain criteria set by your plan administrator. Generally, you can borrow up to 50% of your vested balance, with a maximum cap of $50,000. The repayment period is typically five years, though this can be extended for home purchases.

While a 401(k) loan can be an appealing option, it's not without risks. If you leave your job before the loan is repaid, the outstanding balance may be treated as a taxable distribution and subject to a 10% early withdrawal penalty if you're under 59½. Additionally, the money you borrow will no longer be compounding in the market, potentially affecting your long-term retirement growth.

SUPERCHARGING YOUR SAVINGS AFTER 50

If you're 50 or older, you're actually eligible to make catch-up contributions to your retirement accounts. Catch-up contributions provide an opportunity to close the retirement savings gap. This provision allows older workers to boost their savings during the final stretch of their working years, which can be a game-changer for those who started saving later in life. For example, if you've been focused on paying off debt or raising a family and couldn't contribute as much earlier in life, these extra contributions allow you to make up for lost time.

For 401(k) accounts, the IRS allows an additional contribution of $7,500 in 2024, on top of the standard $22,500 annual limit – due by the due date of your tax return (not including extensions). For IRAs, you can contribute an extra $1,000 beyond the regular $6,500 limit. These additional contributions are tax-advantaged, meaning they reduce your taxable income for the year or grow tax-free in a Roth account.

Over a decade, maxing out your catch-up contributions could add tens of thousands of dollars to your retirement fund – or even more, thanks to compound interest.

TURNING TAXABLE DOLLARS INTO TAX-FREE INCOME

Roth IRAs and Roth 401(k)s offer a unique advantage: tax-free income in retirement. If you have traditional retirement accounts, such as an IRA or 401(k), you can convert some or all of those funds into a Roth account, potentially reducing your future tax liability. You'll pay taxes on the converted amount in the year of the conversion, but the funds grow tax-free after that, and qualified withdrawals in retirement are also tax-free.

Roth conversions make sense if you expect your tax rate in retirement to be higher than it is today. This can be the case if you have significant savings in pre-tax accounts, plan to delay Social Security benefits, or anticipate major medical deductions later in life. Strategic timing is crucial for Roth conversions. Many retirees choose to convert funds during years when their income is lower, such as early retirement before required minimum distributions (RMDs) kick in at age 73.

By spreading conversions over several years, you can potentially save tens of thousands in future taxes while creating a source of tax-free income.

MAXIMIZING YOUR RETIREMENT POTENTIAL

Retirement accounts are more versatile than many people realize. From borrowing against your 401(k) to leveraging catch-up contributions and Roth conversions, there are a lot of ways to optimize your retirement strategy. By taking full advantage, you can better prepare for a financially secure future.

Whether you're just starting to save or nearing retirement, our team is here to provide personalized guidance tailored to your goals. Contact us at info@4-pointfinancial.com or call us at 781-894-0488 to schedule a consultation. Together, we'll craft a retirement strategy that works for you.

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