Young or old, get moving

Editor's note: *Kent Vickre and Dwight Raab write a tax and finance column for each issue of Pioneer* GrowingPoint® *magazine. Vickre is state coordinator of the Iowa Farm Business Association. Raab is state coordinator of Illinois Farm Business Farm Management. They address issues that influence agri-business success.*

It may seem odd to cover funding for retirement and college tuition in the same article. Most people think these two goals generally work against each other. It would appear they'd be difficult to fund simultaneously.

However, they share some similarities: Both topics take a great deal of planning and foresight to fulfill your plans.

Rocking chair prep

Let's start with saving for retirement. If you've already started and are well under way, congratulations. You are one of the few. Still, most of us could do a better job planning for our retirement. If you haven't started, it's not too late. It's better to start late than to not start at all.

Remember, the Social Security Administration never intended that Social Security pensions would be our sole source of income in our retirement years. Social Security provides a base of income during our retirement years, but you will likely need to supplement that income with savings of some sort that you put away in your working careers.

Your Social Security benefit is based on the highest 35 years of contributions. Considering most of us have only a 45-year working career at best, we need every one of those years to count.

IRAs are popular

The most used options for retirement savings are the traditional and Roth IRA. The limit for 2009 contributions to either of these options is $5,000 for those under age 50 and $6,000 for those 50 and older.

If you're not familiar with the difference between the traditional and the Roth IRA, here's a quick lesson. The traditional IRA is a tax-deferred arrangement that lets you deduct from your income the amount you contribute to it, deferring income tax payment until your retirement years (after age 59?). Distributions from a traditional IRA are mandatory.

The Roth IRA does not permit a deduction from current taxable income, but the distributions from a Roth IRA generally are not taxable in your retirement years.

The important part is to get started saving for retirement. With the advantage of time, you can accumulate a sizable amount of savings ... if you start early. If you take away the advantage of time, you must contribute larger amounts to savings. And there are limits on this with an IRA.

> Saving for retirement? Saving for college? Either way, it's best to start early.

It adds up fast

The power of compound interest is truly marvelous. If you were to start saving in earnest at age 25 and contribute $5,000 per year for 20 years to your IRA, the result at 5 percent interest would be $438,669 at age 65. And that's only making contributions for the first 20 of those 40 years.

If you were to wait until age 45 to start saving, you'd need to contribute $13,266 per year for those 20 years to arrive at the same $438,669 at age 65 (again at 5 percent interest).

Other retirement plans offer a higher contribution limit. Those who are self-employed need to consider how they're treating hired labor in their businesses. Some of the retirement plans require you to treat employees and their ability to participate in defined ways. Consult your tax adviser for information on alternative retirement plans, their contribution limits and any limitations on deductions based on income.

If you do get a late start in retirement savings, a good strategy is to delay retirement as long as you can. This might permit you to increase the chances of achieving your retirement goal — even if it comes later rather than sooner.

The same goes for college

That leaves us funding college for our kids. Tuition has risen at a rate much higher than inflation in many parts of the county. This makes planning for college tuition necessary long before the money is needed.

Like funding retirement, when funding college, earlier is better. In 1996, the Internal Revenue Service created section 529 of the Internal Revenue Code. This created what now are called 529 plans. A 529 plan is an education savings plan operated by a state or educational institution designed to help set aside funds for future college and university costs.

These 529 plans can be used to cover costs of qualified colleges and universities nationwide. In most of the 529 plans, your child's choice of school is not affected by the state in which your 529 savings plan originates. You can be a California resident, invest in a Vermont 529 plan and send your student to college in Texas.

Not all colleges and universities are eligible, so check to see if your institution is listed under 529 rules.

Two 529 options

There are two general types of 529 plans. They usually are categorized as either prepaid or savings plans. Savings plans work much like other tax-deferred investment plans by investing your contributions in mutual funds or similar investments. These plans usually offer several investment options from which to choose.

The value of your account will go up or down based on the performance of the particular option you select. Prepaid plans let you prepay all or part of the tuition cost of an in-state public college education. They may also be converted for use at private and out-of-state colleges.

Although contributions to a 529 plan are not deductible on your federal tax return, your investment grows tax-deferred. And, the distributions to pay for the beneficiary's college costs come out federally tax-free. This feature makes them seem much like Roth IRAs. The tax-free treatment was made permanent with the Pension Protection Act of 2006.

The bottom line is this: When funding retirement or college, it's best to start as early as possible. Consider your options, talk to a financial advisor and make adjustments to suit your individual situation.