IRA mistakes to avoid - and get the most bang for your buck

Contributing to an individual retirement account (IRA) can be a tax-advantaged* way to set money aside for your post-career life. As long as you follow a few golden rules to make your money work harder for you, that is. Here, we share five of the most common — and potentially costly — IRA mistakes to avoid.

Mistake #1: Not having an IRA

Nearly anyone with earned income (money made from working, not from Social Security or investments) can open and contribute to an IRA. Even if you don't have a job, you can still have an IRA if your spouse has earned income.

These broad eligibility guidelines and the tax advantages of an IRA make it a strong choice when you're considering long-term retirement investments. It's particularly true if you don't have an employer-sponsored retirement plan.

Mistake #2: Not understanding your options

Each type of IRA treats taxes a little differently, so make sure you understand the differences.

- Traditional IRA — invest pre-tax dollars, lowering your taxable income, and don't pay taxes on earnings until you withdraw the money.
- Roth IRA — pay taxes as usual on the money you contribute; don't pay taxes on the interest you earn once you start making withdrawals.

Mistake #3: Not considering consolidation

If you have multiple IRAs, you might be losing money by paying management fees on each account. By consolidating your accounts into a single IRA, you might save money by paying only one annual fee. Before making a change, compare the cost of any transfer fees against the fees you'll save.

If you do consolidate, use a direct transfer, so you retain tax-deferred status on your assets and avoid federal tax withholdings.

Mistake #4: Not contributing the maximum amount

For 2019, you can contribute up to $6,000 annually to an IRA — $7,000 if you're age 50 or older. (Important: You can open and contribute to an IRA until each year's tax filing day.) Contributing the full amount gives you the opportunity to maximize interest earnings and, with a traditional IRA, potentially minimize your tax bill.

Rather than making the full contribution at one time, many people opt to make regular contributions throughout the year. Setting up an automatic deduction from your checking account helps ensure you stick with your investment commitment.

Mistake #5: Ignoring the risk of penalties

Some of the costliest IRA mistakes can occur if you don't fully understand these three contribution and withdrawal rules:

- If you contribute more than the maximum in any year, you could face a 6% penalty.
- If you withdraw money before age 59-1/2, the funds will be taxed as ordinary income and you could incur a 10% tax. (Some exceptions exist.)
- If you don't withdraw at least the required minimum distribution (RMD) once you reach age 70-1/2, you could be hit with a 50% tax on the amount of the RMD that you didn't withdraw.

More IRA Assistance

To learn more about IRA contribution limits, withdrawal requirements and other

regulations, download IRS Publications 590-A and 590-B.