

Enhancements to Saver's Credit make it more attractive than ever before

American workers don't have the best track record when it comes to saving money for retirement. In fact, they're ranked near the bottom when compared to workers in other industrialized countries. The new Pension Protection Act signed into law last month aims to do something about that. The new law makes permanent a previously temporary - and surprisingly underused - tax credit: the "Saver's Credit."

Dollar-for-dollar tax savings

The Saver's Credit offers individuals some real incentives to save for retirement. It can reduce the federal income tax your employees pay dollar-for-dollar. The amount of the employee's credit is based on the contributions he or she makes and his or her credit rate.

The credit rate can be as high as 50 percent, depending on the employee's adjusted gross income. Generally, the credit rate declines as income rises. The credit rate also depends on the employee's filing status. The amount of the credit cannot exceed the taxpayer's tax liability.

For single taxpayers (and married filing separate or qualifying widow(er)), the Saver's Credit rate is 50 percent of the contribution if AGI is \$0-15,000. The rate is 20 percent if AGI is \$15,001-16,250; 10 percent if AGI is \$16,251-25,000; and zero percent if AGI is above \$25,000.

For married couples filing jointly, the Saver's Credit rate is 50 percent of the contribution if AGI is \$0-30,000. The rate is 20 percent if AGI is \$30,001-32,500; 10 percent if AGI is \$32,501-50,000; and zero percent if AGI is above \$50,000. The AGI amounts for a head of household are three-fourths of the amounts for joint filers.

\$2,000 maximum annual contribution

The maximum annual contribution taken into account for the credit is \$2,000. For married couples filing jointly, the maximum annual contribution taken into account for the credit is \$2,000 for each person. An individual also has to be over age 18, not a full-time student and not claimed as a dependent on another taxpayer's return.

In some cases, the amount of any contribution eligible for the Saver's Credit is reduced by the amount of any taxable distribution received by the taxpayer or by the taxpayer's spouse.

Many types of retirement savings arrangements

The Saver's Credit is available for so many types of retirement savings arrangements that more workers should be taking advantage of it. Salary reduction contributions to the following arrangements are eligible for the Saver's Credit:

- 401(k) plans
- 403(b) annuity plans
- Governmental 457 plans
- SIMPLE IRA

- Salary reduction SEP

A contribution made under an automatic enrollment plan also qualifies. Additionally, contributions to an IRA - traditional and Roth IRAs - are eligible for the Saver's Credit.

Example

Philip and Pauline are married and file jointly. During 2006, Philip elects to have \$2,000 contributed to his employer-sponsored 401(k). Pauline makes a deductible contribution of \$2,000 to an IRA. Combined, their AGI for 2005 is \$29,000. Philip's Saver's Credit rate is 50 percent of his \$2,000 401(k) contribution or \$1,000. Pauline's Saver's Credit rate is also 50 percent of her \$2,000 IRA contribution or \$1,000.

New enhancements

The new pension protection act makes the Saver's Credit even more attractive. First, the Saver's Credit is now permanent. Under old law, it would have expired after 2006. Second - and this is a big improvement - the AGI amounts used to calculate the credit rate will be adjusted for inflation starting in 2007. (Note: The \$2,000 maximum contribution amount is not indexed for inflation.)

Are your employees taking advantage of the Saver's Credit? Our office can help you get the word out to your employees about this valuable tax break. Not only will your employees benefit from saving for the future, they may also receive an immediate tax savings.