Get Ready to Test Your Retirement Planning Smarts

This three-part quiz tests investors' knowledge of saving and investing for retirement.

Retirement planning starts with your first contribution to a retirement account and continues throughout your working years. But how much do you really know about it? Find out by taking our quiz. Answers follow each question, but don't look ahead!

1 Shana and Doug both began working at Super Duper Company at age 25. As soon as she was eligible, Shana started contributing $200 a month ($2,400 a year) to the company's 401(k) plan. She continued contributing until her retirement at age 65. Doug waited until he was 40 to begin making contributions. Then he contributed $400 a month ($4,800 a year) -- twice as much as Shana -- until he reached age 65. Their investments earned a hypothetical average annual return of 7%, compounded monthly.[1]

Who had more money at retirement, Shana or Doug?

Answer: If you chose Doug, you're off the mark by approximately $202,000! Shana's much earlier start gave her two huge advantages: time and the power of compounding (earning income on your original investment and on the earnings it generates). Although she contributed less than Doug -- $96,000 compared with Doug's $120,000 -- Shana had $528,025 saved at retirement, while Doug had only $325,919 (before taking income taxes into account).

1. This example is for illustrative purposes only and is not representative of any particular investment vehicle. Your investment performance will likely differ from the amounts shown. Please evaluate your risk capacity in determining which investments are appropriate for you.

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2 After working at Super Duper Company for 20 years, Soco, Huong, and Calvin were all leaving for other jobs, so they had to decide what to do with the money in their retirement plan accounts. Soco elected to leave her money in Sooper Dooper's 401(k) plan. Huong requested a trustee-to-trustee transfer of his account balance to a rollover individual retirement account (IRA). And Calvin withdrew all his savings in a lump sum so he could pay off his debts.

How did their choices impact their federal income taxes?

Answer: Soco's decision to leave her money in her current plan meant that her savings continued to grow tax deferred until she withdrew her money at retirement.

And because he rolled over his account balance to an IRA, Huong's retirement savings also remained tax deferred. If allowed, Huong could also have avoided taxes on the distribution by rolling the money into his new employer's 401(k) plan.

By taking a lump-sum withdrawal, Calvin received only 80% of his account balance as 20% was withheld to prepay income taxes. And, in his tax bracket, this wasn't the extent of his tax liability. Plus, since Calvin was under age 59½ and wasn't eligible for an exception, he had to pay a 10% additional tax for early withdrawal. Calvin not only wound up with a lot less money than he'd planned on having to pay down his debts, but his retirement savings were also wiped out.

3 Since their employer doesn't offer a retirement plan, coworkers Jack and Helena decided to open IRAs. Jack chose an IRA that allows him to make tax-deductible contributions and enjoy tax-deferred earnings. He won't pay taxes until he withdraws his money. Helena's contributions to her IRA are not deductible. However, she can withdraw her contributions tax free at any time, and withdrawals of earnings will also be tax free after she's reached age 59½, as long as she's met a five-year waiting period.

Which type of IRA -- traditional or Roth -- are Jack and Helena each investing in?

Answer: Jack is investing in a traditional IRA; Helena has a Roth IRA. Both offer tax advantages -- Jack's is immediate since he gains a tax deduction for his contributions, whereas Helena's will be realized later when she takes tax-free withdrawals. But, unlike Jack, Helena won't be required to take annual minimum distributions from her IRA after she reaches age 70½.

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