Here's a smart retirement planning strategy for agents at every level

Regardless of what stage you're at in your real estate career, it's never too early or too late to start building a retirement plan

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As small business owners, real estate agents face unique challenges in accumulating retirement savings, as they do not have the built-in 401k option available like their corporate counterparts. Instead, they must select from a complex menu of tax-advantaged accounts on their own.

To make matters worse, the optimal strategy used for retirement planning may differ depending on the stage of the agent's career. This means agents must be fully aware of the options available to them to ensure they are using the best plan over time to make the biggest impact on their financial future.

In this article, we'll break down an agent's career into four stages and identify the financial tools that should be utilized at each stage to build an effective real estate agent retirement plan.

Stage No. 1: 'The rookie'

At this point in their career, agents are just starting out and may not have a lot of extra income to invest. For this reason, a Traditional IRA is an excellent option for retirement planning. Although it may not be a lot, consistent investing is essential to build strong financial habits even at the earliest stage of an agent's career.

Compound interest is powerful, and the earlier agents can start accumulating retirement assets, the more growth they will experience over their careers. A Traditional IRA is the simplest account to set up, and it allows real estate agents to contribute up to $6,000 per year ($7,000 if over 50). The contributions will likely be tax-deductible for a rookie agent, but it's essential to verify this with a CPA or adviser.

If eligible to deduct an IRA contribution, the tax deduction will lower the agent's taxable income, resulting in a lower tax bill.

Stage No. 2: 'The sophomore'

As "sophomores," agents have established themselves, and their GCI (gross commission income) has grown to a point where they have the desire to save for retirement at a rate that an IRA cannot provide with its low contribution limits. Agents need to look at more advanced retirement accounts available only to small business owners to find more room to save. The SEP-IRA is an excellent option for retirement planning at this stage.

A SEP IRA allows real estate agents to contribute up to 25 percent of their income or $61,000, whichever is less. The contributions are tax-deductible and will help lower the agent's taxable income. This is especially beneficial for "sophomore" real estate agents who are starting to climb into higher income tax brackets.

The way that tax savings are calculated depends on the marginal income tax bracket that an agent falls into. That means, the higher the GCI, the higher the tax bracket and the higher the tax impact a retirement contribution will make. Saving to a tax-advantaged retirement account becomes more and more lucrative as an agent's business grows.

Stage No. 3: 'The veteran'

As real estate agents continue to build their businesses, successful agents will soon find themselves in the "veteran" stage of their careers. "Veteran" agents have established a successful business and are making a significant income. They are also paying a significant tax bill.

In an effort to combat the tax situation, a common tax-planning strategy that agents implement by this stage is making an S Corp election with their LLC. While this can be a great move from a tax planning perspective, it can also significantly limit the retirement savings of an agent if they are still relying on a SEP IRA.

In this scenario, a Solo 401k is an excellent option for retirement planning. A Solo 401k allows real estate agents to contribute up to $61,000 per year ($67,000 if over 50), and the contributions are tax-deductible. While the limits are largely the same as a SEP, the big difference from a SEP IRA is that real estate agents can make contributions as both the employee and the employer, which will more than likely result in higher contribution limits if they have an S Corp.

As seen throughout the stages, the ability to contribute more to retirement accounts is especially beneficial for real estate agents looking to maximize their tax savings.

Stage No. 4: 'The team'

In our final stage, successful real estate agents have established a thriving real estate team with employees. As the account title "solo" 401k implies, this plan isn't suitable for agents with a team of employees. Therefore, a custom 401k plan is an excellent retirement planning option.

A custom 401k plan allows real estate agents to collaborate with a financial professional who specializes in designing retirement plans tailored to the unique needs of their team, such as contribution matching for employees and other customized features. However, it's important to note that this complexity may come at an additional cost.

As a result, it likely does not make financial sense to pay for a custom 401k plan with all the bells and whistles until you reach this stage in your career.

Many lower-cost options are available until you have employees. Nonetheless, if you find yourself in this position, implementing a custom 401k plan can be an excellent solution for both your financial success and your team's financial well-being.

Closing thoughts

In conclusion, retirement planning is crucial if you want to start building assets for retirement and reap significant tax benefits along the way. Unfortunately, agents often neglect or underutilize this important aspect of financial planning as they progress through their careers.

Regardless of what stage you're at, it's never too early or too late to start building a retirement plan. If you feel overwhelmed by the options or unsure about which stage you're in, don't hesitate to seek the help of a financial professional to guide you in choosing the right plan.