INDIVIDUAL RETIREMENT ACCOUNTS IN GENERAL

There are two types of individual retirement accounts (IRAs). They are 1) conventional IRAs and 2) Roth IRAs. Contributions to both types of IRAs are subject to earned income limitations. Additionally, Roth IRA contributions can be limited based on a taxpayer's AGI.

Roth IRA contributions are not deductible. A deduction is allowed for contributions to conventional IRAs. This deduction may be limited if a taxpayer participates in a pension plan at work. There is never a limitation on conventional IRA contributions as long as the earned income test is met.

The maximum annual contribution limitations discussed below are per taxpayer and not per type of IRA. Example: An individual under the age of 50 can make a maximum IRA contribution during 2018 of $5,500. This can be to a conventional IRA, a Roth IRA, or a combination of contributions to both types of IRAs as long at the annual contribution to all IRAs does not exceed $5,500.

INDIVIDUAL RETIREMENT ACCOUNTS - CONVENTIONAL IRAS

In General

Distributions from individual retirement accounts (IRAs) are included in taxable income unless a portion of the distribution represents prior IRA contributions that were not deductible.

Generally, IRA contributions are deductible in arriving at adjusted gross income. The deductions for IRA contributions for higher-income taxpayers that participate in an employer sponsored pension plan may be limited.

Taxpayers may always make IRA contributions in amount equal to the lesser of earned income or $5,500 ($6,500 for taxpayers over age 50). If a taxpayer participates in a pension plan at work the deduction maybe reduced or eliminated. The income earned on nondeductible IRA investments is not taxed until distributed.

Taxpayers are required to pay a 10 percent excise tax on IRA distributions made before attaining the age of 59 1/2 (early distributions). This excise tax is in addition to any income tax associated with the distribution.

Taxpayer's are required to take distributions from IRAs when the reach the age of 70 1/2. The required amount of the distribution is generally calculated as the value of the IRA(s)/taxpayer's life expectancy. Married taxpayers may elect to use a joint life expectancy.

Detailed Discussion - contributions and deductions

Individual retirement account contributions are generally deductible up to a maximum of $5,500 per year ($6,500 per year for taxpayers over age 50). Married taxpayer's filing a joint return can generally each deduct up to $5,500 per year of individual retirement account contributions ($6,500 for each individual over age 50).

There are limits placed on allowable IRA contributions and deductible IRA contributions. These rules are discussed below. It is possible to make an IRA contribution even if the contribution is not deductible. The earnings generated from deductible and nondeductible IRA contributions are not taxed until a taxpayer receives distributions from an IRA account.

The maximum IRA contribution is limited by a taxpayer's earned income (generally wages and net earnings from self-employment). A taxpayer cannot make an IRA contribution in excess of earned income. However, a working spouse can contribute for a non-working spouse if the working spouse has earned income of at least the total of both contributions. The deductibility of the spousal IRA maybe limited based on the rules discussed below. The contribution of a non-working spouse must be made into an IRA account in the name of the non-working spouse.

Limitations are placed on IRA deductions for individuals who participate in a pension plan at work. The deductible IRA contribution is phased out when a single individual's adjusted gross income is more than $63,000 and less than $73,000 and when a married individual's adjusted gross income is more than $101,000 and less than $121,000. (Note: the $101,000 threshold is for married individuals filing a joint return where both spouses participate in a pension plan at work). If an individual's spouse participates in a pension plan at work but the individual does not participate in a pension plan at work the threshold amount is $189,000 and the deduction is completed eliminated at $199,000 for the spouse not covered by a pension plan at work. The reduction in the maximum IRA deduction is calculated as follows:

The amount over the threshold divided by $10,000 ($20,000 on MFJ returns where both spouses participate in a pension plan at work) x $5,500 (or $6,500 for taxpayers over age 50).

The threshold amounts are:

Single	$63,000
MFJ both spouses participate in a pension plan	$101,000
MFJ where on spouse participates in a pension plan	$189,000

Examples:

Married filing jointly, AGI of $104,000, both taxpayers are under age 50 and participate in a pension plan at work. The reduction in the amount of deductible IRA contributions is calculated as follows: (104,000-101,000=3,000; 3,000/20,000 x 5,500 = $825). Each taxpayer's maximum deductible IRA contribution is reduced by $825. If both taxpayers elect to make a $5,500 IRA contribution, $4,675 would be deductible and $825 would be nondeductible. If either or both taxpayer(s) elected to make a $4,800 IRA contribution, $125 be nondeductible and $4,675 would be deductible. Note: always use the maximum allowable contribution ($5,500 or $6,500) when calculating the reduction.

Married filing jointly, spouse 1 (s1) participates in a pension plan at work and spouse 2 (s2) does not. If AGI is $147,000, s1's allowable IRA deduction is zero; s2's allowable IRA deduction is $5,500 ($6,500 if S2 is over age 50). S1 could make a $5,500 ($6,500 if S1 was over age 50) of nondeductible contribution (assuming that s1 has at least $5,500 or $6,500 of earned income).

Married filing jointly, spouse 1 (s1) participates in a pension plan at work and spouse 2 (s2) does not. If AGI is $194,000, s1's allowable IRA deduction is zero; s2's allowable IRA deduction is reduced because joint AGI is above the threshold amount ($189,000). The reduction of the deductible contribution is calculated as follows; ($194,000-189,000=5,000; 5,000/10,000 x 5,500 = $2,750). The maximum deductible IRA contribution for s2 is reduced by $2,750. S2 could make a $5,500 contribution, $2,750 would be deductible, and $2,750 would be nondeductible. If S2 was over the age of 50, then maximum contribution is $6,500; $3,250 would be deductible and $3,250 would not be deductible (calculated as $194,000-189,000=5,000/10,000 x 6,500= 3,250).

Excise tax on early distributions

Taxpayers are required to pay a 10 percent excise tax on IRA distributions made before attaining the age of 59 1/2 (early distributions).

Taxpayers may withdraw funds from an IRA to pay for higher educational expenses of the taxpayer or the taxpayer's spouse, dependents, or grandchildren. Distributions from IRAs that are used to pay for higher educational expenses are not subject to the 10% excise tax associated with retirement account distributions occurring before a taxpayer reaches the age of 59 1/2.

First-time homebuyers may withdraw up to $10,000 from an IRA and avoid the 10% excise tax on early IRA distributions. Distributions must be used to purchase a home within 120 days.

Other distributions not subject to the 10% penalty include:

1. Distributions after the taxpayer's death,

2. Distributions because of the taxpayer's disability,

3. Distributions in the form of substantially equal periodic payments for the life (or life expectancy) of the owner of an IRA, or the owner and his beneficiary,

4. Distributions resulting from an IRS levy, or

5. Distributions to individuals called to active duty

ROTH IRAS

Taxpayers may make Roth IRA contributions of $5,500 per year ($6,500 for taxpayers over age 50) and are subject to the same earning limitations as conventional IRAs discussed above. Roth IRA contributions are always nondeductible. Distributions (including the earnings on contributions) from Roth IRAs are nontaxable as long as funds are withdrawn after a taxpayer has reached the age of 59 1/2 and 5 years has past since the taxpayer first made a Roth IRA contribution. A taxpayer can be penalized for Roth IRA distributions made after the age of 59 1/2 if 5 years have not passed since a taxpayer first made a Roth IRA contribution. For purposes of the five-year rule, a contribution for any given year is considered made on the first day of the year.

Roth IRA distributions that are subject to tax because the tax-free distribution requirements were not met are considered made in the following order:

1) from initial contributions (these distributions are not taxed because no deduction was allowed when the contribution was made),

and then

2) From earnings.

The taxable portion of early distributions from Roth IRAs is also subject to a 10% excise tax unless one of the following exceptions is met.

Distribution is made to a beneficiary because of a taxpayer's death

Distribution is made because taxpayer is disabled.

Distribution is made for the purchase of a first residence. ($10,000 maximum, see notes under conventional IRAs for more details regarding this exception).

The 10% excise tax will apply to distributions meeting the above exceptions if the five-year rule discussed above is not met.

The allowable Roth IRA contribution is phased out for single taxpayers with adjusted gross income of $120,000-$135,000 and married taxpayers with adjusted gross income of

$189,000-$199,000. If a taxpayer's AGI is above the phase-out amount, no contribution is available. Allowable contributions based on income are rounded to the next $10 amount. Example: MFJ, both spouses age 48 with AGI of $190,000. The allowable Roth IRA contribution is computed as follows. AGI over threshold $1,000 ($190,000 - $189,000) / $10,000 x $5,500 = $550. The allowable IRA contribution for each spouse is $4,950 (computed as $5,500 - $550).

	Conventional IRA	Roth IRA
CONTRIBUTIONS	maximum yearly contribution 5,500 (6,500) over age 50 (1) limited by earned income spousal IRA rules can by-pass earned income test	maximum yearly contribution 5,500 (6,500) over age 50 (1) limited by earned income spousal IRA rules can by-pass earned income test subject to AGI limitations
DEDUCTIONS	no limitation if no participation in work pension plan limits based on AGI imposed if taxpayer participates in work pension plan AGI limits different on MFJ return bases on spouse's participation in work pension plan	never deductible
INCOME TAXATION DISTRIBUTIONS	earnings always taxed contributions taxed if previously deducted if nondeductible contributions were made % of each dollar distributed is taxed (2)	not taxed if 5 year and 59 1/2 age test met if distribution is taxable contributions are distributed first (nontaxable) then earning (100% taxable)
10% EXCISE TAX EARLY DISTRIBUTIONS	applies to taxable portion of distributions occurring prior to age 59 1/2 penalty tax (10% excise tax) is in addition to income taxes imposed on distributions exceptions to 10% tax based on use (3)	applies to taxable portion of distributions occurring prior to age 59 1/2 penalty tax (10% excise tax) is in addition to income taxes imposed on distributions exceptions to 10% tax based on use (3)

(1) The maximum yearly contribution is per taxpayer and includes contributions to all IRA's. Total contributions to Conventional and/or Roth IRAs cannot exceed the maximum of 5,50 or 6,500 (age 50+) per tax year

(2) nontaxable portion of distribution is determined by dividing nondeductible contributions by total IRA value

(3) exception applies only to 10% penalty tax and does not affect income taxation of distribution; exceptions to penalties based on use of funds are not the same for conventional and Roth IRAs