IRA Opportunities

Traditional IRAs
Roth IRAs

Questions & Answers

What is the purpose of this brochure?

It explains the contribution limits for traditional IRAs and Roth IRAs. It also explains the new IRA contribution credit.

Traditional IRA

What is a traditional Individual Retirement Account (traditional IRA)?

A traditional IRA is a special tax-deferred savings account authorized by Internal Revenue Code section 408. It is a unique and simple way to encourage people to save money for retirement.

What are the tax benefits realized from a traditional IRA?

Generally you may add up to $3,000 or $3,500 for 2004, or $4,000 or $4,500 for 2005, of earned income to your IRA account each year and have it be either fully or partially tax deductible (see Deductibility Chart). If your contribution is tax deductible, then you receive two tax benefits: 1) an immediate tax savings because you will pay fewer taxes because of the deduction and 2) the earnings generated by the IRA funds are not taxed until distributed. If your contribution is not tax deductible, you still receive the tax benefit of tax deferral on the IRA's earnings. You may also qualify for a tax credit.

When do I have to establish the traditional IRA?

You have until the due date (without extensions) for filing your federal income tax return, normally April 15, to establish and fund your traditional IRA for the previous tax year.

Am I eligible to contribute to a traditional IRA?

You are eligible for a regular contribution if you do not reach age 70½ in the calendar year for which you wish to make the contribution, and you have compensation (income earned from performing material personal services). You may also qualify for a rollover or a transfer contribution.

How much am I eligible to contribute to my traditional IRA for the 2004 tax year if I will NOT be at least age 50 as of December 31, 2004?

You are eligible to contribute the lesser of 100% of your compensation, or $3,000 (2004) or $4,000 (2005), as reduced by any amount you contributed to your Roth IRA for the same tax year.

How much am I eligible to contribute to my traditional IRA for the current tax year if I will be at least age 50 as of December 31?

You are eligible to contribute the lesser of 100% of your compensation, or $3,500 (2004) or $4,500 (2005), as reduced by any amount you contributed to your Roth IRA for the same tax year.

May I contribute to my traditional IRA and also my Roth IRA for the same year?

Yes, but you are subject to the applicable contribution limit for such year.

What are the contribution limits for a person who is not age 50 or older?

Tax Year	Amount
2004	$3,000
2005-2007	$4,000
2008-2010	$5,000

What are the contribution limits for a person who is age 50 or older?

Tax Year	Amount
2004	$3,500
2005	$4,500
2006-2007	$5,000
2008-2010	$6,000

May my spouse or I use the spousal IRA contribution rules to make a contribution to our respective traditional and/or Roth IRA?

Yes. You (or your spouse) will be eligible to make a spousal contribution to a either IRA if the following rules are satisfied:

- You and your spouse must each have your own traditional and/or Roth IRA.
- You must be married as of the end of the tax year (i.e. December 31).
- You must file a joint income tax return.
- You must have compensation includible in gross income which is less than that of your spouse.

Your annual IRA contribution will be limited to the lesser of (1) $3,000, $3,500, $4,000 or $4,500, as applicable;

or (2) the sum of your compensation which is includible in gross income for such year plus the compensation of your spouse as reduced by your spouse's contribution to his or her own traditional IRA and Roth IRA.

To what extent will I be entitled to a tax deduction for my IRA contribution?

The answer depends upon your filing status, whether or not you and/or your spouse is covered by an employer-sponsored retirement plan at work, and your modified adjusted gross income (AGI).

If you are single and you are not covered under an employer-sponsored retirement plan, then you are entitled to a full deduction to the extent of your contributions, regardless of your income.

If you are married and neither you nor your spouse is covered under an employer-sponsored retirement plan, then you are entitled to a full deduction to the extent of your contributions, regardless of your income.

If you are covered under an employer-sponsored retirement plan and your filing status is single or head of household, then you are entitled to a deduction as follows. A full deduction as long as your MAGI is $45,000 or less for 2004, and $50,000 or less for 2005. A partial deduction for 2004, since the maximum allowable contribution is ratably phased out, if you have modified adjusted gross income between $45,000 and $55,000. A partial deduction for 2005, since the maximum allowable contribution is ratably phased out, if you have modified adjusted gross income between $50,000 and $60,000. You are not allowed any deduction if your MAGI for 2004 is $55,000 or more, and for 2005, no deduction is allowed if your MAGI is $60,000 or more.

If you are covered under an employer-sponsored retirement plan and your filing status is married, filing jointly or as a qualifying widower, then you are entitled to a deduction as follows. A full deduction as long as your MAGI is $65,000 or less for 2004, and $70,000 or less for 2005. A partial deduction for 2004, since the maximum allowable contribution is ratably phased out, if you have modified adjusted gross income between $65,000 and $75,000. A partial deduction for 2005, since the maximum allowable contribution is ratably phased out, if you have modified adjusted gross income between $70,000 and $80,000. You are not allowed any deduction if your MAGI for 2004 is $75,000 or more, and for 2005, no deduction is allowed if your MAGI is $80,000 or more.

If you are not covered under an employer-sponsored retirement plan, but your spouse is, and your filing status is married, filing jointly, then you may be entitled to a partial deduction, or in some cases, no deduction. For 2004 and 2005, the maximum allowable contribution is ratably phased out if you and your spouse's income is between $150,000 and $160,000. No deduction is allowed if your MAGI is $160,000 or greater. A full deduction is allowed if your MAGI is less than $150,000.

If you are married and your filing status is married, filing separately, then you will be entitled to only a partial deduction, or in some cases, no deduction. For 2004 and 2005, the maximum allowable contribution is phased out if you have modified adjusted gross income between $0 and $10,000. No deduction is allowed if your MAGI is $10,000 or greater.

Can I make nondeductible contributions to a traditional IRA?

Yes. You may make nondeductible contributions when you are unable to claim a tax deduction.

Roth IRA

What is a Roth Individual Retirement Account (Roth IRA)?

A Roth IRA is a type of tax-preferred savings and investment account authorized by Internal Revenue Code section 408A. The Roth IRA allows you to accumulate assets for retirement purposes and for other purposes.

What are the tax benefits realized from a Roth IRA?

A Roth IRA will produce tax-free income if certain rules are met. You or your beneficiary(ies) will not be required to include in income, for income tax purposes, a distribution paid from a Roth IRA, whether it be the return of a contribution or the account's earnings, if certain rules are met. In some cases, you may be eligible to claim a tax credit because of your Roth IRA contribution.

What is the basic concept of a Roth IRA, and what are the associated tax benefits?

If you are eligible, you may make contributions, within limits, to the Roth IRA. You make these contributions with after-tax dollars. The earnings realized by the Roth IRA are not presently taxed, and if certain distribution rules are met, will never be taxed. For example, if you are age 42 on January 1, 2004, and you contribute $1,000 a year for 34 years (2004-2037) to a Roth IRA, then your contributions of $34,000 would accumulate to $110,434.88 as of December 31, 2037, if an earnings rate of 6% compounded annually was realized. You and your beneficiary(ies) would, of course, not pay any federal income tax on the contribution amount of $34,000 when distributed, because you cannot claim a tax deduction for your contributions. However, the great tax benefit to be realized from a Roth IRA is that you and your beneficiary(ies) will not have to include in your taxable income the earnings of $76,434.88 (and subsequent future earnings) when distributed to you or your beneficiary(ies) as long as the distributions are qualified distributions as defined later.

When do I have to establish the Roth IRA?

You have until the due date (without extensions) for filing your federal income tax return, normally April 15, to establish and fund your Roth IRA for the previous tax year.

Am I eligible to contribute to a Roth IRA?

You are eligible if you satisfy the following two requirements: (1) you must have earned income or compensation; and (2) you meet certain income limitations. Be aware that you are eligible to make contributions to a Roth IRA even though you are age 70½ or older. For a given year, you may be ineligible to contribute to a Roth IRA, but still be eligible to contribute to a traditional IRA and/or the Coverdell ESA.

What are the income limits for eligibility purposes?

If your income (and your spouse's income, if you are married) is too high, you will not be eligible to make a contribution to a Roth IRA. If you are single, you become ineligible when your adjusted gross income is $110,000 or greater. If you are married, and file a joint return, you become ineligible when the combined adjusted gross income (AGI) of you and your spouse is $160,000 or greater. If you are married and file a separate return, you become ineligible when your adjusted gross income is $10,000 or greater.

Roth IRA Contribution Chart

Amount of AGI and Filing Status

Single, Head of Household or Qualifying Widow(er)

Below $95,000	Entitled to full contribution amount
$95,000-$109,999	Entitled to prorated contribution amount – use special formula*
$110,000 or over	No contribution permissible

*Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $95,000/$15,000. This will give you a ratio that determines the amount you cannot contribute. Round to the lowest $10.00.

Married Filing Jointly

Below $150,000	Entitled to full contribution amount.
$150,000-159,999	Entitled to prorated contribution amount – use special formula.*
$160,000 or over	No contribution permissible.

*Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $150,000/$10,000. This will give you a ratio that determines the amount you cannot contribute. Round to the lowest $10.00.

Married Filing Separate Returns

$0-$9,999	Entitled to prorated contribution amount – use special formula*
$10,000 or Over	No contribution permissible

*Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $0/$10,000. This will give you a ratio that determines the amount you cannot contribute. Round to the lowest $10.00.

How much am I eligible to contribute to my Roth IRA for the 2004 and 2005 tax year if I will NOT be at least age 50 as of December 31, 2004?

You are eligible to contribute the lesser of 100% of your compensation, or $3,000, (2004) and $4,000 (2005) as reduced by (1) application of the special income and filing status limitation rule and (2) any amount you contributed to your traditional IRA for the same tax year.

How much am I eligible to contribute to my Roth IRA for the 2004 tax and 2005 year if I will be at least age 50 as of December 31, 2004?

You are eligible to contribute the lesser of 100% of your compensation, or $3,500, (2004) and $4,500 (2005) as reduced by (1) application of the special income and filing status limitation rule and (2) any amount you contributed to your traditional IRA for the same tax year.

How is my allowable contribution to a Roth IRA calculated?

There is a special formula which must be used, as described in the "Roth IRA Contribution Chart." The formula is as follows:

$$\frac{\text{AGI-Threshold}}{\text{Phaseout Level - Threshold Level}} = \text{Ineligible Contribution Percentage}$$

Tax-Filing Status	Threshold Level	Phaseout Level
Single	$95,000	$100,000
Married/Joint Return	$150,000	$160,000
Married/Separate Return	$0	$10,000

The result is the percentage which **cannot** be contributed to the Roth IRA. You must then apply this percentage to the maximum contribution amount and then subtract this amount from the allowed contribution amount to get the amount which you **can** contribute.

Example — Bob and Lynn Brown have adjusted gross income of $154,000 in 2004, and file a joint tax return. They wish to make contributions to Roth IRAs. How much can each contribute to a Roth IRA? Using the formula for a married taxpayer, filing jointly:

Step 1 $154,000 - $150,000/$10,000
Step 2 $4,000 ÷ $10,000 = .4
Step 3 $3,000 X .4 = $1,200
(**Note: $3,000 is used, not $6,000)**
Step 4 $3,000 - $1,200 = $1,800

This formula must be calculated separately for each spouse, but is based on their combined income. Bob and Lynn could each contribute up to $1,800 to a Roth IRA in 2004, for a total contribution amount of $3,600. They could not contribute $3,000 to one of their Roth IRAs and $600 to the other. When a couple is between the threshold and phaseout levels, the calculated amount must be contributed equally to each of their Roth IRAs in order to maximize the contribution for the year. (They could contribute less than $1,800 to either Roth IRA, but not more.)

May I contribute to a Roth IRA after I have attained age 70½?

Yes, there is no age limit requirement for making contributions to a Roth IRA. The only requirement is that you must have earned income for the year for which the contribution is made.

May I roll over or convert part or all of my traditional IRA to a Roth IRA?

Maybe. Only certain people qualify for such a rollover or conversion.

In order to roll over or convert traditional IRA funds to a Roth IRA, you must have adjusted gross income of $100,000 or less in the year of the rollover, and if married, you must file a joint tax return. Special warning: The IRS has stated that they construe the Code section 408A(c)(3)(B) requirement that the taxpayer's adjusted gross income must not exceed $100,000 to mean that the combined adjusted gross income of persons who are married and who file a joint return must not exceed $100,000.

There are three ways to accomplish a conversion from a traditional IRA to a Roth IRA.

Method #1. An amount distributed from a traditional IRA is contributed (i.e. rolled over) to a Roth IRA within 60 days of the distribution.

Method #2. An amount in a traditional IRA is transferred to a Roth IRA maintained by the same custodian or trustee.

Method #3. An amount in a traditional IRA is transferred in a custodian/trustee-to-custodian/trustee transfer from the custodian/trustee of the traditional IRA to the custodian/trustee of the Roth IRA.

Whatever conversion method is used, the custodian/trustee of the traditional IRA will prepare a Form 1099-R to report the distribution, and the custodian/trustee of the Roth IRA will prepare a 5498 to report the conversion contribution.

Why might I want to convert my traditional IRA to a Roth IRA?

You may find it advantageous to incur the tax consequences of a present distribution in order to qualify to earn the right to have no taxation when the earnings are ultimately distributed from the Roth IRA.

What are the tax consequences of receiving a distribution from a traditional IRA and "converting" the distribution to a Roth IRA?

In general, the amount distributed to you from your traditional IRA will be included in your income in the year of receipt and will be subject to income taxes for that year. The 10% premature distribution excise tax, however, will not be owed even if you are younger than age 59½.

To what extent may I be entitled to a new tax credit for my IRA contributions for the 2004-2006 tax years?

You may be eligible for a new tax credit for contributions you make to your traditional and/or Roth IRA. A formula is used to calculate your credit. Your credit may vary from $1 to $1,000, depending on the amount you contribute to your IRA, your filing status and your modified adjusted gross income. If you meet the following requirements for a given tax year, then you will qualify for this new credit:

1. Be at least 18 years of age as of December 31 of such year.
2. Not be a dependent on someone else's tax return
3. Not be a student as defined in Internal Revenue Code section 25B(c)
4. Have adjusted gross income under certain limits which are based on your filing status:

Joint filers	$50,000.01
Head-of-Household	$37,500.01
All other filers (including Married, filing separately)	$25,000.01

5. Must not have received certain distributions which disqualify you from claiming the credit, or certain distributions which were made to your spouse.

Because of the complexity of this credit, you will want to review IRS Publication 590 for a complete explanation.

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