<u>Individual Retirement Accounts (IRAs)</u>

This handout is provided for informational purposes only and does not replace the advice of a financial professional.

What is a traditional IRA? A traditional IRA allows you to invest on a tax-deferred basis. This means that you do not pay taxes on the amount you contribute or earnings until you retire. This allows you to invest the income taxes you would have paid for decades. When you retire, *you pay taxes on <u>both</u> your contributions and earnings*.

What is a Roth IRA? Unlike a traditional IRA, contributions to a Roth IRA are non-deductible. This means that taxes are paid before the money is invested. However, *any withdrawals from a Roth IRA are tax-free (with exceptions noted on next page).*

Which IRA is better? Traditional or Roth. The deciding factor is the tax rate (percentage) you pay. If you expect to pay a lower tax rate in retirement, it makes better sense to take the deduction now using a Traditional IRA, because you will get more of a tax break. If you expect to pay a higher tax rate in retirement, a Roth IRA will be better because it allows you to avoid paying taxes at that time. Moral: Pay your taxes when the rate is lowest.

Can anyone establish a Roth IRA? For 2023, any single person with (adjusted gross) income less than $153,000, or married couple with income less than $228,000, can establish a Roth IRA *(limits are adjusted annually and may differ if you have a retirement plan at work)*. Sole proprietors, partners and full or part-time employees are eligible. You may establish a Roth IRA even if you participate in a qualified pension, profit sharing or other retirement plan. This is not the case with a traditional IRA.

Are there age limits with a Roth IRA? There is no age limit. A child with earned income can have a Roth IRA and you can contribute to a Roth IRA regardless of how old you are. You simply need earned income to contribute.

What is the maximum contribution to a Roth IRA? For 2023 and 2024, you can contribute up to $6,500 and $7,000, respectively, or 100% of your income whichever is less ($7,500 and $8,000, respectively - if age 50 or older). Contributions can be made until April 15th of the following year.

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Is there a minimum contribution to a Roth IRA? The law doesn't require any minimum. Many banks and mutual fund families will open an account for small amounts since they anticipate having your business for years to come.

Can I make withdrawals from my Roth IRA? Since Roth IRA contributions are made after you pay your taxes, you may withdraw these contributions – tax and penalty free. This is not possible with a traditional IRA.

Is there a limit to the amount that can be withdrawn from a Roth IRA? When you take money out of a Roth IRA, the first dollars you withdraw are considered to be a return of your contributions. You don't have to meet any special tests to receive those dollars free of tax. You can take them out without paying tax or penalties. If you exhaust your contributions and receive a distribution of earnings from your Roth IRA, you are required to pay tax (and possibly penalties) unless you receive a qualified distribution.

What is a qualified distribution? A qualified distribution is a distribution that satisfies two tests: 1) the distribution occurred five years after you establish your Roth IRA, and 2) a type of distribution test. You must meet both of these tests.

What types of distributions qualify? Even after you meet the five-year test, only certain types of distributions are treated as qualified distributions. They are:

1) Distributions made on or after the date you reach age 59 ½.

2) Distributions made to your beneficiary after your death.

3) If you become disabled, distributions attributable to your disability.

4) For birth of child or adoption.

5) $10,000 for qualified first-time homebuyer distributions.

What's the "catch" on first time home purchases? There is none. As long as the Roth IRA has met the five-year test, you can make penalty-free withdrawals to apply toward buying a home. The withdrawals must be used for qualified first home expenses, and there is a lifetime limit of $10,000 on withdrawals for this purpose. A first-time homebuyer does not mean you have never owned a home. It is defined as not owning a home in the last two years.

Need more info? www.irs.gov (Publication 590-A)