PacificCPE

Roth IRAs

Course #3171A

Taxes

2 Credit Hours

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ROTH IRAS

This course describes the benefits of a Roth IRA as compared to its traditional counterpart. The course also covers contribution limits, eligibility requirements, rules for converting one type of IRA into another, and rules governing the withdrawal of funds.

LEARNING ASSIGNMENTS AND OBJECTIVES

As a result of studying each assignment, you should be able to meet the objectives listed below each individual assignment.

SUBJECTS

Introduction to Individual Retirement Accounts
Comparing Roth and Traditional IRAs
Eligibility and Contribution Rules for Roth IRAs
Converting IRAs
Roth IRA Distributions
Roth 401(k) Plans

Study the course materials from pages 1 to 67

Complete the review questions at the end of each chapter

Answer the exam questions 1 to 10

Objectives:

- Identify the key characteristics of traditional IRAs.
- Identify the similarities and differences between Roth and traditional IRAs.
- Recall the contribution rules for Roth IRAs.
- Recall the requirements for converting a traditional IRA to a Roth IRA.
- Identify the taxation rules of Roth IRA distributions.
- Recognize the differences between a designated Roth 401(k) account and a Roth IRA.

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EXAM OUTLINE

- **TEST FORMAT:** The final exam for this course consists of 10 multiple-choice questions and is based specifically on the information covered in the course materials.

- **ACCESS FINAL EXAM:** Log in to your account and click Take Exam. A copy of the final exam is provided at the end of these course materials for your convenience, however you must submit your answers online to receive credit for the course.

- **LICENSE RENEWAL INFORMATION:** This course qualifies for **2** CPE hours.

- **PROCESSING:** You will receive the score for your final exam immediately after it is submitted. A score of 70% or better is required to pass.

- **CERTIFICATE OF COMPLETION:** Will be available in your account to view online or print. If you do not pass an exam, it can be retaken free of charge.

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CHAPTER 1: INTRODUCTION TO INDIVIDUAL RETIREMENT ACCOUNTS

Chapter Objective
After completing this chapter, you should be able to: • Identify the key characteristics of traditional IRAs.

I. TRADITIONAL IRAs

Simply put, a traditional Individual Retirement Account (IRA) is any IRA that is not a Roth IRA or a SIMPLE IRA. An individual is eligible to establish an IRA if he or she received taxable compensation during the year. Prior to January 1, 2020, an individual was unable to contribute if he or she was age 70½ or older. For 2020 and later, there is no age limit on making regular contributions to a traditional IRA.

Individuals are eligible for a traditional IRA whether or not they are covered by any other retirement plan. However, individuals may not be able to deduct all of their contributions if they or their spouse are covered by an employer retirement plan. If both an individual and his or her spouse have compensation, each may establish an IRA. However, spouses cannot participate in the same IRA.

A qualified individual may establish a traditional IRA at any time. However, the time for making contributions for any year is limited. This topic is discussed in more detail below.

A. COMPENSATION

For purposes of being eligible to make an IRA contribution – either Roth or traditional – compensation is what an individual earns from working. Compensation includes, but is not limited to, the following items.

1. <u>Wages and Salaries</u>

Wages, salaries, tips, professional fees, bonuses, and other amounts received for providing personal services are compensation. The IRS treats as compensation any amount properly shown in box 1 of Form W-2 (Wages, tips, other compensation) provided that amount is reduced by any amount properly shown in box 11 (Nonqualified plans). Scholarship and fellowship payments are compensation for IRA purposes only if shown in box 1 of Form W-2. However, for tax years beginning after 2019, certain non-tuition fellowship and stipend payments not reported to the individual on Form W-2 are treated as taxable compensation for IRA purposes. These amounts include taxable non-tuition fellowship and stipend payments made to aid the individual in the pursuit of graduate or postdoctoral study and included in the individual’s gross income.

2. Commissions

Any amounts received that are a percentage of profits or sales price is compensation.

3. Self-employment Income

If an individual is self-employed (a sole proprietor or a partner), compensation is the net earnings from his or her trade or business (provided the individual's personal services are a material income-producing factor) reduced by the total of:

- The deduction for contributions made on his or her behalf to retirement plans; and
- The deduction allowed for one-half of his or her self-employment taxes.

In addition, compensation includes earnings from self-employment even if they are not subject to self-employment tax because of a person's religious beliefs.

4. Alimony and Separate Maintenance

For IRA purposes, compensation includes any taxable alimony and separate maintenance payments received under a decree of divorce or separate maintenance, but only with respect to divorce or separation instruments executed on or before December 31, 2018 that have not been modified to exclude such amounts.

5. Nontaxable Combat Pay

If an individual was a member of the U.S. Armed Forces, compensation includes any nontaxable combat pay he or she received. This amount should be reported in box 12 of the individual's 2022 Form W-2 with code Q.

6. Graduate or Postdoctural Study

A scholarship or fellowship is generally taxable compensation only if it is in box 1 of the individual's Form W-2. However, for tax years beginning after 2019, certain non-tuition fellowship and stipend payments not reported to the individual on Form W-2 are treated as taxable compensation for IRA purposes. These amounts include taxable non-tuition fellowship and stipend payments made to aid the individual in the pursuit of graduate or postdoctoral study and included in the individual's gross income.

TABLE 1.1 COMPENSATION FOR PURPOSES OF AN IRA

Note. These rules apply to both traditional and Roth IRAs.

Items Considered Compensation	Items Not Considered Compensation
• Wages, salaries, etc. • Commissions • Self-employment income • Taxable alimony and separate maintenance • Non-taxable combat pay • Taxable non-tuition fellowship and stipend payments	• Earnings and profits from property • Interest and dividend income • Pension or annuity income • Deferred compensation • Income from certain partnerships • Any amounts excluded from income

B. TYPES OF INDIVIDUAL RETIREMENT ACCOUNTS

Different types of IRAs can be established with a variety of organizations. Individuals can set up an IRA at a bank or other financial institution or with a mutual fund or life insurance company. Individuals can also open an IRA through a stock broker. Any IRA must meet Internal Revenue Code requirements. A traditional IRA can be an individual retirement account or annuity. It can be part of either a simplified employee pension (SEP) or an employer or employee association trust account.

1. Individual Retirement Account

An individual retirement account is a trust or custodial account set up in the United States for the exclusive benefit of the individual or his or her beneficiaries. The account is created by a written document. The document must show that the account meets certain technical requirements. Contributions, except for rollover contributions, must be in cash. In addition, assets in the individual's account cannot be combined with other property, except in a common trust fund or common investment fund. Account holders must start receiving distributions by April 1 of the year following the year in which they reach age 72. [**Note:** Individuals who reach age 72 after December 31, 2022, may delay receiving their RMDs until April 1 of the year following the year in which they turn age 73.]

2. Individual Retirement Annuity

An individual may establish an individual retirement annuity by purchasing an annuity contract or an endowment contract from a life insurance company. An individual retirement annuity must be issued in the owner's own name, and either that individual or the beneficiaries who survive the individual are the only ones who can receive the benefits or payments.

An individual retirement annuity must meet all the following requirements:

- The account holder's entire interest in the contract must be nonforfeitable;
- The contract must provide that the account holder cannot transfer any portion of it to any person other than the issuer;