ROTH IRAs

Roth IRAs are tax-favored accounts and one way to set aside funds for retirement. In order to fund a Roth IRA, an individual must have earned income, and there are certain income requirements in order to be eligible to contribute. These contributions are not tax-deductible, but earnings grow tax-deferred and distributions are tax-free. These accounts started in 1998 as part of the Taxpayer Relief Act of 1997.

FEATURES

CONTRIBUTIONS

For 2015, the maximum contribution is $5,500 and is made with after-tax dollars. Individuals age 50 or older by year-end may make an additional $1,000 "catch-up" contribution and those filing jointly can contribute $11,000 if under age 50, or $13,000 if both are age 50 or older by the end of the year.

ELIGIBILITY REQUIREMENTS

For this year, the eligibility requirements to contribute to a Roth IRA are:

- For single filers and those filing as a head of household, if their modified AGI is under $116,000, they are allowed to contribute to a Roth IRA. If their income is between $116,000 and $131,000, they are able to make a reduced contribution, and for those with AGIs over $131,000, they are not eligible to make a Roth IRA contribution.
- For those filing jointly or a qualifying widower, if their modified AGI is under $183,000, they can each make a Roth IRA contribution. For AGIs between $183,000 and $193,000, they can contribute a reduced amount, and if their AGI is over $193,000, they are not eligible to make a Roth IRA contribution.

CONTRIBUTION DEADLINE

Contributions to a Roth IRA can be made any time during the year or up to the tax filing deadline for that year, not including extensions. Contributions that exceed the contribution limit and are not withdrawn by the due date for the tax return for that year are considered excess contributions and are subject to a 6% "excess contribution" tax.

DISTRIBUTIONS

Distributions from Roth IRAs are generally not taxable. They must be a qualified distribution and meet the following requirements:

1. It is made after the 5-year period beginning with the first taxable year for which a contribution was made to a Roth IRA set up for your benefit, and

2. For Roth Contributory IRAs, the distribution of earnings is one of the following:
   - Made on or after the date you reach age 59 ½.
   - Made because you are disabled.
   - Made to a beneficiary or to your estate after your death.
   - One that meets certain requirements in purchasing your first home.

However, Roth IRA contributions can be withdrawn at any time. The above rules and applicable penalty must be taken into account when withdrawing any earnings. Distributions of earnings not meeting the above conditions are subject to a 10% penalty.

ROTH CONVERSIONS

Traditional IRAs and dormant 401(k) plans can be fully or partially converted to Roth IRAs, potentially offering future tax benefits to account holder and beneficiary. Any pre-tax contributions and all earnings that are converted are considered taxable income in the year of the conversion, but future distributions from the Roth IRA will be tax free. For 2015, anyone can partake in a Roth IRA conversion regardless of income. However, one should take into consideration what tax bracket they are currently in, whether the taxable portion of the conversion will raise them to a higher tax bracket, and what tax bracket they expect to be in when they begin withdrawing funds from the Roth IRA.

ROTH CONVERSION DEADLINE

Conversions must be done by December 31st in order to count for the current year. In the event an individual wants to reverse their conversion (due to market downward movement, tax liability, etc.), he or she can “re-characterize” or undo their conversion. This re-characterization must be completed by October 15th of the following year without paying any tax or penalty.

REQUIRED MINIMUM DISTRIBUTIONS

Roth IRAs are generally not subject to Required Minimum Distributions (RMDs). An exception to this rule, however, is when a non-spousal beneficiary inherits a Roth IRA. They must either withdraw all the funds within five years or take required minimum distributions over their expected lifetime.