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Answers to Your Roth IRA Questions

Q. What is a Roth IRA?

A. The Roth IRA is an individual retirement account created by the Taxpayer Relief Act of 1997.

Q. How does the Roth IRA work?

A. Contributions to your Roth IRA are never tax-deductible. However the money in your Roth IRA, including earnings, can be withdrawn tax-free, provided you conform to the plan provisions.

Q. Am I eligible to contribute to a Roth IRA?

A. Anyone is eligible who has income from compensation (or who is filing jointly with a spouse who earns compensation) with the following modified adjusted gross income (MAGI):

Up to \$95,000 (single filers)

Up to \$150,000 (joint filers)

Reduced contributions allowed for higher incomes, up to \$110,000 for single filers and \$160,000 for joint filers.

Q. How much is the full Roth IRA Contribution?

A. The amount of a full Roth IRA contribution varies. If you meet the eligibility requirements and you are under age 50, you can contribute up to \$3,000 for 2004, and \$4,000 for 2005 through 2007. If you have attained age 50 by the end of a year, then your limits are \$3,500 for 2004, \$4,500 for 2005, and \$5,000 for 2006 through 2007.

Q. What happens if my (our) income is too high to make a full contribution to a Roth IRA?

A. A portion of the full contribution can be made if your MAGI is between \$95,000 and \$110,000 for single filers, and between \$150,000 and \$160,000 for joint filers. When income exceeds \$110,000 for single filers and \$160,000 for joint filers, a regular Roth IRA contribution can't be made for that year.

Q. Can I get any tax credits for making IRA contributions?

A. You may be able to receive a tax credit for making contributions for the 2002 through 2006 tax years. The full credit is 50 percent of the first \$2,000 of contributions. The full credit is available for joint filers who have joint MAGI up to \$30,000, heads of households with MAGI up to \$22,500, or other filers with MAGI up to \$15,000. Smaller tax credits are available for joint filers with MAGI up to \$50,000, heads of households with MAGI up to \$37,500, or other filers with MAGI up to \$25,000.

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Q. Can I still contribute to a Roth IRA if I participate in an employer-sponsored retirement plan?

A. Yes, and you can contribute past age 70½ as long as you continue to earn compensation.

Q. Will my Roth IRA affect the amount that I can contribute to my employer-sponsored retirement plan?

A. No. The amount you contribute to your 401k or other employer-sponsored plans will not be affected by your Roth IRA. However, you must conform to the plan contribution limits for your employer-sponsored plan.

Q. Can I have both a Traditional and a Roth IRA?

A. Yes, you can maintain both types of IRAs at the same time. You can even make contributions to both types of IRAs in the same year. But your contributions to both Roth and Traditional IRAs cannot exceed the maximum contribution limit for all IRAs.

Q. When can I start taking tax-free distributions from my Roth IRA?

A. You can withdraw most contributions without paying income tax at any time. There are two requirements to qualify for tax free withdrawals of the income your Roth IRA has earned. First, your Roth IRA must meet the “five-year test.” In other words, it must be five years after the first year for which Roth contributions were made. Second, one of the following must apply:

- a) You are over age 59½
- b) Funds are going to your beneficiary upon your death
- c) You have become disabled
- d) You are using the funds for a first-time home purchase (lifetime limit is \$10,000 per person)

If you have made a conversion contribution , please read further for taxation issues regarding conversions in this situation.

Q. What if I make an early withdrawal from my Roth IRA and I am not age 59½ or covered by any exception.

A. If you make early withdrawals from a Roth IRA to which you have only made regular contributions of up to \$2,000 per year, the amounts are considered to come from your already-taxed contributions first, with no additional taxes or penalties due. When you begin to withdraw earnings from the account, this money will be subject to ordinary income taxes, plus an additional 10 percent early distribution tax.

Q. Do I have to take minimum distributions when I reach age 70½?

A. No. You are not required to start taking minimum distributions when you reach age 70½. If you don't need the cash, you can let your money continue to grow tax-free for as long as you like. However, minimum distributions must be made to your beneficiaries following your death.

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Q. Can I convert my existing Traditional IRA to a Roth IRA?

A. Yes. You can convert your Traditional IRA to a Roth IRA if your MAGI in the year of the conversion is under \$100,000. This limit is the same for both single filers and married couples who file jointly. Married taxpayers who file separately are not eligible for a Roth conversion. Use care and be sure to get all the facts. This is a complicated decision.

Q. Does the IRA conversion contribution ceiling of \$100,000 MAGI include the IRA conversion amount?

A. No. The MAGI is calculated prior to adding the amount of the IRA conversion contribution.

Q. If I convert a Traditional IRA to a Roth IRA, do I owe any taxes?

A. Yes. Upon conversion, you will owe ordinary income taxes on your investment earnings and on deductible contributions you have made to your Traditional IRA. This amount is taxable income in the year the money leaves the Traditional IRA. Basically, you owe tax on any money that has not been taxed before. But you will have the opportunity to withdraw earnings made after the conversion, free of any taxes.

Q. What about penalties on conversions from Traditional to Roth IRAs?

A. The 10 percent early withdrawal penalty is waived on IRA conversions.

Q. Are there different tax rules regarding withdrawals of IRA conversion contributions?

A. A distribution that is attributed to an IRA conversion contribution is not subject to income tax. If the distribution is made within five years after the conversion, then the 10 percent early withdrawal tax applies unless there is an exception.

Q. Can my Roth IRA be inherited?

A. Yes. Upon your death, the entire proceeds can be passed on tax-free to your beneficiaries, once the five-year test has been met. This means there may be a delay before your beneficiaries will be able to receive the income earned within the Roth IRA on a tax-free basis.

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