TAX YEAR
2018

Financial Planning Guide

Personal Financial Planning

Budgeting

Steps to manage income and expenses include the following.

- Identify monthly outflows as living expenses, savings, and discretionary. Eliminate unnecessary expenses from the discretionary category. If further cuts need to be made, reduce living expenses by obtaining a less expensive auto or home. Reduce savings as a last resort. Track income and expenses monthly and review every six months.
- Establish an emergency fund equal to six months of income saved.
- Save on private mortgage insurance by putting at least 20% down on a home mortgage.

Education Funding

Several tax advantages are available to help save for education expenses.

- Savings bond interest may be tax free if used for qualified education expenses.
- Coverdell education savings accounts (ESAs) provide tax-deferred growth and tax-free distributions for qualified education expenses.
- Qualified Tuition Programs (529 plans) provide tax-free distributions for qualified tuition expenses.
- A gift of low-basis stock allows the individual's child to sell the stock and use the proceeds to fund education expenses. This is beneficial when the individual is in a higher tax bracket and the student is in a lower tax bracket.
- Roth IRAs can be used as a savings vehicle for education purposes. Contributions are removed from a Roth IRA without tax or penalty. Parents and grandparents fund the Roth IRA with the intention of removing the contribution and gifting that amount to the student. If the student does not go to college, or has the costs covered by other means, the contributions can stay in the Roth IRA without concern for tax or penalty.
- Cash-value life insurance can also be used as a funding mechanism for college expenses.

Insurance

The purpose of insurance is to transfer the risk of loss to a third party to prevent catastrophic financial loss should that risk become a reality. For this reason, people choose to insure the larger risks and take on the smaller potential losses at their own risk.

- Liability insurance protects from financial loss due to specific incidents that create a liability. Automobile and homeowner insurance are examples of insurance that provide liability protection.
- Health insurance provides financial protection from medical costs associated with illness and/or injury.
- Disability insurance provides for income replacement in the event a person is unable to work due to injury or illness.
- Long-term care insurance protects financial assets and income in the event a person is confined to a long-term nursing home or needs in-home care for an extended period of time.
- Life insurance provides for an immediate lump-sum amount of money in the event of the insured's death. The purpose of life insurance is to provide income replacement in the event the income earner dies.

➲ ***Planning Tip:*** *Individuals should ask their auto and home insurance agent about purchasing umbrella liability protection. The cost is economical and it can provide additional protection from a liability loss.*

Financial Planning Guide

Investment Planning

Stocks, bonds, money markets, mutual funds, commodities, real estate, and options are the most common types of investments. Most financial professionals will recommend diversifying an investment portfolio across the different spectrum of investments. Investors need to be aware of the risks involved with any investment.

- ***Market risk.*** This is the risk that the value of the investment will be below the purchase price when or if it needs to be sold.
- ***Inflation risk.*** If the increase in value of an investment is less than the increase in the inflation rate, the future purchasing power will be less.
- ***Liquidity risk.*** Not all investments can be sold at a moment's notice. Some investments do not have a marketplace where they can be sold.
- ***Interest rate risk.*** If an individual buys an interest-bearing investment and interest rates go up, the current investment value can decrease.
- ***Tax risk.*** Buying and selling repeatedly for a profit will lead to taxable gains. The tax paid presents a risk to the investment value.
- ***Political risk.*** Specifically, when investing globally, political changes within a country can decrease investment values.
- ***Currency risk.*** Fluctuations in world currencies will cause investment values to rise or fall, independent from the true value of the investment.

Income Tax Planning

In addition to the economic logic that a financial transaction must have, it is important to evaluate the tax consequences of those transactions.

Basis and Holding Period

Knowing the basis and holding period in advance of a transaction can prevent costly tax consequences. Selling highly-appreciated assets will increase the amount of tax owed. Selling investments that are below basis can provide tax benefits by allowing a dollar-for-dollar reduction against capital gains. In addition, individuals are allowed to write off investment losses in excess of gains up to $3,000 per year. Any amount not used can be carried forward to future tax years.

Example: *Val owns the following shares of stock.*

	Stock A	*Stock B*	*Total*
Cost	$1,000	$3,000	$4,000
FMV	$4,000	$1,000	$5,000
Unrealized gain/loss	$3,000	($2,000)	$1,000

Val wants to make a $5,000 charitable donation by selling her stock and contributing the cash to charity. If she sells both stocks and donates the proceeds, she will generate a taxable capital gain of $1,000 and take a charitable deduction of $5,000. Instead of selling both stocks, Val could gift stock A to the charity, along with the proceeds from the sale of stock B. Her tax result would be a capital loss of $2,000 from the sale of stock B and a charitable deduction of $5,000 ($4,000 FMV of stock A, plus $1,000 proceeds from the sale of stock B). She thus avoids paying tax on the $3,000 appreciation on stock A while achieving the same charitable deduction.

Annuity or Life Insurance Exchanges

A life insurance or annuity contract can be exchanged to a different life insurance or annuity contract without the exchange becoming taxable. Limitations may apply.

Early Retirement

Early retirees (before age 59½) are allowed to take distributions from retirement plans and avoid the 10% additional tax. In order to do so, they must follow certain rules.

- Distributions must be taken at least annually in substantially equal amounts.
- Distribution amounts are determined by life expectancy of the recipient.
- Distributions must be taken for a minimum of five years beginning with the year of the first distribution. If, at the end of the five years, the recipient has not yet attained the age of 59½, he or she must continue the distributions until attaining age 59½.

Contact Us

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- Pension or IRA distributions.
- Significant change in income or deductions.
- Job change.
- Marriage.
- Attainment of age 59½ or 70½.
- Sale or purchase of a business.
- Sale or purchase of a residence or other real estate.
- Retirement.
- Notice from IRS or other revenue department.
- Divorce or separation.
- Self-employment.
- Charitable contributions of property in excess of $5,000.

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Early Retirement Distributions — SEPP

Early Retirement Distributions

A taxpayer may choose, or be forced into choosing, early retirement. A retirement before age 59½ creates income challenges for the retiree. The retiree is not yet eligible to receive retirement benefits from Social Security. The retiree may or may not have a monthly pension to generate income.

In many situations, the retiree will need to generate income from his or her assets. Often, the retiree has most of his or her assets in a retirement plan through a 401(k) plan at his or her employer or in an individual retirement arrangement (IRA). Withdrawals of earnings and pre-tax contributions are subject to ordinary income tax. In addition, taxpayers may be subject to the 10% early withdrawal penalty tax on distributions taken before the taxpayer reaches age 59½.

Tax Summary

- Withdrawals of earnings and pre-tax contributions from an IRA are subject to ordinary income tax.
- Unless an exception applies, taxable withdrawals from an IRA prior to age 59½ are subject to a 10% early withdrawal penalty.
- Taxpayers who take a series of substantially equal periodic payments from an IRA are not subject to the 10% additional tax.

Tax Planning Strategy

One strategy to generate income from retirement accounts for taxpayers under age 59½ is to take periodic distributions from those accounts. If structured properly, the 10% additional tax will not be assessed on the distributions. Taxpayers can take distributions from various retirement accounts such as 401(k) plans, 403(b) plans, and IRAs.

Substantially Equal Periodic Payments (SEPP)

The Internal Revenue Code allows taxpayers to take withdrawals from retirement accounts without incurring the 10% penalty. To do so, very specific rules need to be followed.

- The payments made to the taxpayer from the IRA are based on one of three calculation methods.
- The payments must be made to the taxpayer at least annually during the payment years. Payments can be made more frequently, such as monthly, but the total for each year during the SEPP period must meet the payment calculation result for the year or years during the SEPP.
- Payments must be made for a period of at least five years or until the taxpayer reaches age 59½, whichever is later.

Example: *Fred, age 52, establishes a SEPP from his IRA. He must continue to take withdrawals until he reaches age 59½. If he discontinues or changes his SEPP withdrawals at any time before he reaches age 59½, the current year withdrawal is subject to the additional 10% tax. In addition, the SEPP withdrawals for previous years are retroactively subject to the additional 10% tax. If, however, Fred begins SEPP withdrawals at age 58, he must continue the withdrawals to age 63 to comply with the 5-year withdrawal requirement.*

Calculation Method

Payments are considered to be substantially equal periodic payments if they are made in accordance with one of the three calculation methods allowed.

Early Retirement Distributions — SEPP

1) Required minimum distribution method. Under this method, the account balance, the number from the life expectancy table, and the resulting annual payment amount is re-determined each year.
2) Fixed amortization method. The annual payment for each year is determined by amortizing in level amounts the account balance over a specified number of years determined using a life expectancy table and a chosen interest rate. Under this method, the annual payment is determined once for the first distribution year and the annual payment is the same in each succeeding year.
3) Fixed annuitization method. The annual payment for each year is determined by dividing the account balance by an annuity factor that is the present value of an annuity of $1 per year beginning at the taxpayer's age and continuing for the life of the taxpayer. The annuity factor is derived from a mortality table and a chosen interest rate. Under this method, the annual payment is determined once for the first distribution year and the annual payment is the same amount in each succeeding year.

One-Time Change to Required Amount

A taxpayer who begins distributions in a year using either the amortization method or the annuitization method may in any subsequent year switch to the required minimum distribution method to determine the payment for the year of the switch and all subsequent years. The change in method will not be treated as a modification. Once a change is made, the required minimum distribution method must be followed in all subsequent years until the required number of years under the plan have been met.

Changes to Account Balance

No other contributions or distributions can be taken from the account being distributed from during the SEPP period. This includes nontaxable transfers in or out of the account.

Example: *Susan establishes a SEPP distribution from her IRA. Two years later, at age 53, she takes on a new job and wants to make contributions to an IRA with her newly earned income. Susan cannot contribute to the IRA that is making her SEPP distribution. Susan can establish a new, separate IRA account that she can make contributions to.*

Depletion of Account Value

If, as a result of following an accepted method of determining SEPP withdrawals, a taxpayer's IRA assets are exhausted, the taxpayer will not be subject to the additional income tax of 10%. The resulting cessation of payments will not be treated as a modification of the series of payments.

Example: *Dick established a SEPP distribution plan at age 54 that required him to take a distribution amount of $25,000 each year. He invested aggressively in his SEPP account and, due to distributions and declines in the stock market, the value of his account was down to $15,000 when Dick took his distribution at age 58. Because the account has been depleted, none of the amounts distributed through the SEPP plan in prior years is subject to the 10% additional tax. In addition, the $15,000 distribution at age 58 is not subject to 10% additional tax. Also, because the account has been depleted, he will face no tax consequences for not being able to take a distribution at age 59.*

Possible Risks

- The rules for distributions using the Internal Revenue Code provide very little flexibility. Once the distribution begins, taxpayers need to exert extreme caution in making any changes to the distribution amount and frequency.
- Taxpayers need to document the calculations used to determine the distribution, as well as any change in distribution. Tax courts have consistently assessed the 10% additional tax for taxpayers who could not substantiate the distributions were, in fact, based on SEPP calculations.

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Individual Retirement Accounts

Backdoor Roth IRA

Backdoor Roth IRA

Generally, you can only contribute to a Roth IRA if you have taxable compensation and income less than the top of the phaseout range for your filing status (see chart below). If your income is greater than that threshold amount, you are prohibited from contributing directly to a Roth IRA.

A "backdoor Roth IRA" allows a taxpayer to bypass income limitations by first making a nondeductible contribution to a traditional IRA and then converting it into a Roth IRA. If the conversion happens soon after the original contribution, there will be little or no taxable income or tax assessed. Due to the distribution rules for traditional IRAs, this works best if you have no other traditional IRAs.

Roth IRA Limits—2018	
Individual Contribution Limits	
Under age 50	$5,500
Age 50 or older	$6,500
Roth IRA Phaseouts	
MFJ or QW	$189,000 to $199,000
Single, HOH, or MFS (did not live with spouse at any time during the year)	$120,000 to $135,000
MFS (live with spouse at any time during the year)	$0 to $10,000

Nondeductible Contributions

Generally, if you are prohibited from making a direct Roth IRA contribution, you are phased out from making a deductible traditional IRA contribution as well. Therefore, in order to make a backdoor Roth IRA contribution, you would first make a nondeductible contribution to a traditional IRA. Nondeductible contributions are considered to be made with money you have already paid tax on, or "after tax." Shortly after making a nondeductible contribution to a traditional IRA, you can convert the traditional IRA to a Roth IRA.

Conversions

You can withdraw all or part of the assets from a traditional IRA and reinvest them in a Roth IRA. The amount that you withdraw and timely contribute (convert) to the Roth IRA is called a conversion contribution. If properly rolled over, the 10% additional tax on early distributions will not apply. However, a part or all of the distribution from your traditional IRA may be included in gross income and subjected to ordinary income tax.

There are no income limitations on converting a traditional IRA into a Roth IRA. The conversion is treated as a rollover, regardless of the conversion method used.

Conversion method. You can convert amounts from a traditional IRA to a Roth IRA in any of the following three ways.

- ***Rollover.*** You can receive a distribution from a traditional IRA and roll it over (contribute it) to a Roth IRA within 60 days after the distribution.
- ***Trustee-to-trustee transfer.*** You can direct the trustee of the traditional IRA to transfer an amount from the traditional IRA to the trustee of the Roth IRA.
- ***Same trustee transfer.*** If the trustee of the traditional IRA also maintains the Roth IRA, you can direct the trustee to transfer an amount from the traditional IRA to the Roth IRA. Conversions made with the same trustee can be made by redesignating the traditional IRA as a Roth IRA, rather than opening a new account or issuing a new contract.

Individual Retirement Accounts

Backdoor Roth IRA

Conversion of deductible IRA. If you convert a traditional IRA that you received a tax deduction on in a previous year to a Roth IRA, you will owe taxes on the entire amount converted.

Example: *Jaslyn has a traditional IRA with a fair market value of $500,000. All of the contributions to the traditional IRA were deductible. If Jaslyn convert's the entire $500,000 traditional IRA to a Roth IRA, she will owe ordinary income taxes on the full $500,000 amount.*

Conversion of nondeductible IRA. If you make a nondeductible contribution to a traditional IRA, you can convert the entire amount tax-free. Only the earnings on the nondeductible IRA contributions are taxed.

Example: *Manny is single and has a modified AGI of $250,000. He wishes to save money in a Roth IRA so he can make nontaxable withdrawals upon retirement. In 2018, he opens a traditional IRA with a $5,500 nondeductible contribution and a couple months later, converts it to a Roth IRA. He has no other traditional IRAs. At the time of Roth conversion, the account had increased in value by $250, which is the only taxable part of the conversion.*

Conversion of part-deductible/nondeductible IRA. If you make a conversion to a Roth IRA that consists of deductible and nondeductible IRA contributions, you will owe tax on the proportion of your overall IRA balance that is considered after tax (nondeductible) as compared to before tax (deductible). You cannot choose to have the cost basis distributed first. Additionally, the values of all traditional IRAs are aggregated to determine the taxable portion of a distribution. Each distribution is partly nontaxable and partly taxable until your entire cost basis has been distributed.

Because of these traditional IRA distribution rules, the backdoor Roth IRA works best if you do not have any other traditional IRAs.

Example: *Jay has $100,000 in his traditional IRA, $10,000 of which is after-tax. Therefore, 10% ($10,000 ÷ $100,000 = 10%) of his traditional IRA consists of after-tax money. If Jay wants to convert $20,000 of his traditional IRA to a Roth IRA, $2,000 ($20,000 × 10% = $2,000) would be tax free. The remaining $18,000 ($20,000 – $18,000 = $2,000) would be taxable.*

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Example: *Gloria has $95,000 in her traditional IRA, all of which is pre-tax. If Gloria makes a $5,000 nondeductible (after-tax) contribution to a traditional IRA, her total IRA balance will be $100,000, $5,000 of which will be after-tax. Thus, only 5% ($5,000 ÷ $100,000 = 5%) of her Roth IRA conversion will be tax-free. If Gloria converts $5,000 from her traditional IRA to a Roth IRA after making her nondeductible contribution, just $250 would be tax free ($5,000 × 5%), while the remaining $4,750 ($5,000 – $250 = $4,750) would be taxable.*

Required Minimum Distribution (RMD)

You cannot convert amounts that must be distributed from your traditional IRA for a particular year (including the calendar year in which you reach age 70½) under the required distribution rules.

Periodic Distributions

If you started taking substantially equal period payments from a traditional IRA, you can convert the amount in the traditional IRA to a Roth IRA and then continue the periodic payments. The 10% additional tax on early distributions will not apply even if the distributions are not qualified distributions, as long as they are part of a series of substantially equal periodic payments.

Recharacterization

A conversion of a traditional IRA to a Roth IRA, and a rollover from any other eligible retirement plan to a Roth IRA, made in tax years beginning after December 31, 2017, cannot be recharacterized back into a traditional IRA. Accordingly, a recharacterization cannot be used to unwind a Roth IRA conversion.

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- Self-employment.
- Charitable contributions of property in excess of $5,000.

Individual Retirement Accounts
Traditional IRAs

Traditional IRAs

IRA Contribution Limits—2018	
Lesser of: Taxable compensation for the year, or:	
Under age 50	$5,500
Age 50 or older	$6,500

What is an IRA?

An IRA is an individual retirement arrangement. It is a personal savings plan that gives you tax advantages for setting aside money for retirement. An IRA is referred to as a traditional IRA if it is not a Roth IRA or a SIMPLE IRA. Traditional IRAs include SEP IRAs.

Traditional IRA tax advantages and rules:

- Contributions to an IRA may be fully or partially deductible.
- Amounts in your IRA (including earnings and gains) are not taxed until distributed.
- There is no limit on how much you can earn and still contribute (however, contributions are not deductible above certain amounts).
- Contributions are not allowed past age 70½ and required minimum distributions begin after age 70½.
- Early distributions (before you are age 59½) are subject to a 10% additional tax. Exceptions apply.
- Distributions are taxed as ordinary income.

Who Can Contribute to an IRA?

Any individual can set up a traditional IRA if he or she receives taxable compensation during the year and is not age 70½ by the end of the year. An individual can have a traditional IRA even if covered by an employer-sponsored retirement plan. However, the deductible amount of contributions to a traditional IRA may be phased out. See *Reduced IRA Deduction*, later.

Compensation for IRA Purposes

Includes	*Does Not Include*
• Wages, salaries, tips, professional fees, bonuses, and other amounts received for providing personal services. • Commissions. • Self-employment income. • Nontaxable combat pay. • Alimony and separate maintenance payments. • Taxable scholarship and fellowship payments are compensation for IRA purposes.	• Earnings and profits from property, such as rental income. • Interest and dividend income. • Pension or annuity income. • Deferred compensation. • Income from certain partnerships. • Conservation Reserve Program (CRP) payments. • Any amounts (other than combat pay) excluded from income.

Contribution limit. Contributions to IRAs are limited to the lesser of the individual's compensation (or spouse's compensation under a spousal IRA), or $5,500 ($6,500 for age 50 or older).

Total contributions are combined with Roth IRA contributions to determine limits. For example, a $1,000 contribution to a Roth IRA will reduce total contributions allowable to a traditional IRA by $1,000.

Spousal IRA. If both spouses have compensation, each can set up a separate IRA. Spouses cannot participate in the same IRA. If filing status is Married Filing Jointly and one spouse's compensation is less than the contribution limit, the lower-income spouse can use the compensation of the other spouse to qualify. However, the spousal IRA is limited to total compensation reduced by any IRA contributions.

This means that the total combined contributions that can be made for the year to your IRA and your spouse's IRA can be as much as $11,000 ($12,000 if only one of you is age 50 or older or $13,000 if both of you are age 50 or older).

70½ rule. Contributions cannot be made in a year the participant has reached age 70½ or for any later year.

Individual Retirement Accounts

Traditional IRAs

When Can You Make Contributions?

Contributions to an IRA can be made at any time during the year or by the due date of your return for that year (not including extensions). This means that most people can make contributions for 2018 by April 15, 2019.

How Much Can You Deduct?

Generally, you can deduct the lesser of:

- The contributions to your traditional IRA for the year, or
- The general limit (or spousal limit) for the year.

However, if you or your spouse is covered by an employer retirement plan, you may not be able to deduct this amount.

Covered by an employer retirement plan. If you or your spouse was covered by an employer retirement plan at any time during the year for which contributions were made, your deduction may be limited. Limits on the amount you can deduct do not affect the amount that can be contributed. Box 13, Form W-2, will be checked if you are covered.

Reduced IRA Deduction

Subject to whether you or your spouse was covered by an employer retirement plan, you may be entitled to only a reduced (partial) deduction or no deduction at all, depending on your modified adjusted gross income (MAGI) and filing status.

MAGI. MAGI for IRA purposes is your adjusted gross income (AGI) from line 37, Form 1040, plus any traditional IRA deduction, student loan interest deduction, foreign earned income or housing exclusion, U.S. Savings Bond interest exclusion, employer-provided adoption benefits exclusion, domestic production activities deduction, or tuition and fees deduction.

2018 IRA Phaseouts—Taxpayer Covered by a Retirement Plan at Work

Filing Status	*MAGI*	*Deduction Allowable*
Single or Head of Household	$63,000 or less.	A full deduction.
	More than $63,000 but less than $73,000.	A partial deduction.
	$73,000 or more.	No deduction.
Married Filing Jointly or Qualifying Widow(er)	$101,000 or less.	A full deduction.
	More than $101,000 but less than $121,000.	A partial deduction.
	$121,000 or more.	No deduction.
Married Filing Separately (use Single if you did not live with spouse at any time during the year)	Less than $10,000.	A partial deduction.
	$10,000 or more.	No deduction.

2018 IRA Phaseouts—Neither Covered by Retirement Plan at Work

Filing Status	*MAGI*	*Deduction Allowable*
Single, Head of Household, or Qualifying Widow(er)	Any amount.	A full deduction.
Married Filing Jointly or Married Filing Separately	Any amount.	A full deduction.

2018 IRA Phaseouts—Taxpayer Not Covered, but Spouse Covered by Retirement Plan at Work

Filing Status	*MAGI*	*Deduction Allowable*
Married Filing Jointly	$189,000 or less.	A full deduction.
	More than $189,000 but less than $199,000.	A partial deduction.
	$199,000 or more.	No deduction.
Married Filing Separately (You are entitled to a full deduction if you did not live with your spouse at any time during the year)	Less than $10,000.	A partial deduction.
	$10,000 or more.	No deduction.

Required Minimum Distribution (RMD)

The RMD is the minimum amount that you must withdraw each year upon reaching age 70½. You may withdraw more than the minimum required amount. The withdrawals will be included in taxable income except for any part that was already taxed or can be received tax free.

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TAX YEAR
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Individual Retirement Accounts
Roth IRAs

Roth IRAs

Roth IRA Contribution Limits—2018

Lesser of: Taxable compensation for the year, or:

Under age 50	$5,500
Age 50 or older	$6,500

What is a Roth IRA?

A Roth IRA is an individual retirement arrangement. It is a personal savings plan that gives you tax advantages for setting aside money for retirement. An account must be designated as a Roth IRA when opened.

Roth IRA tax advantages and rules compared to a traditional IRA:

- Contributions are not deductible. Active participation in an employer plan is irrelevant.
- If certain requirements are satisfied for qualified distributions, distributions are tax free.
- Can withdraw contributions any time for any reason without owing taxes or penalties.
- Contributions can be made after the participant reaches age 70½.
- The required minimum distribution (RMD) rules do not apply. Distributions are not required until death of the participant.
- Contributions are not allowed when modified adjusted gross income (MAGI) is above certain limits.
- Neither a SEP IRA nor a SIMPLE IRA can be set up as a Roth IRA.

Who Can Contribute to a Roth IRA?

Generally, you can contribute to a Roth IRA if you have taxable compensation and income less than the top of the phaseout range for your filing status, see *Roth IRA Phaseouts* chart, next column.

Roth IRA Phaseouts—2018

Filing Status	*MAGI*	*Contribution Limit*
Single, Head of Household, or Married Filing Separately (did not live with spouse any time during the year)	Less than $120,000.	Up to $5,500 ($6,500, age 50 and older).
	At least $120,000, but less than $135,000.	Contribution limit reduced.*
	$135,000 or more.	Cannot contribute to Roth IRA.
Married Filing Jointly or Qualifying Widow(er)	Less than $189,000.	Up to $5,500 ($6,500, age 50 and older).
	At least $189,000, but less than $199,000.	Contribution limit reduced.*
	$199,000 or more.	Cannot contribute to Roth IRA.
Married Filing Separately (lived with spouse at any time during the year)	Zero.	Up to $5,500 ($6,500, age 50 and older).
	More than zero, but less than $10,000.	Contribution limit reduced.*
	$10,000 or more.	Cannot contribution to Roth IRA.

*To calculate reduced contribution limit:
1) Subtract the lower limit of the phaseout range from MAGI.
2) Divide result by $10,000 (MFJ and MFS, lived with spouse) or $15,000 (all others).
3) Multiply result by maximum contribution amount.
4) Subtract the result from the maximum contribution limit.

Bob, age 35, Single, $124,000 MAGI:
1) $124,000 – $120,000 = $4,000.
2) $4,000/$15,000 = 0.27.
3) 0.27 × $5,500 = $1,485.
4) $5,500 – $1,485 = $4,015 (Bob's maximum contribution limit).

Compensation. Compensation includes wages, salaries, tips, professional fees, bonuses, and other amounts received for providing personal services. It also includes commissions, self-employment income, nontaxable combat pay, military differential pay, and taxable alimony and separate maintenance payments.

Contributions. Total contributions are combined with traditional IRA contributions to determine limits. For example, a $1,000 contribution to a traditional IRA will reduce total contributions allowable to a Roth IRA by

Individual Retirement Accounts

Roth IRAs

$1,000. Employer contributions under a SEP or SIMPLE IRA plan do not affect this limit.

If your modified AGI is within the phaseout amounts, your contribution limit is gradually reduced.

When Can You Make Contributions?

You can make contributions to a Roth IRA for a year at any time during the year or by the due date of your return for that year (not including extensions). This means that most people can make contributions for 2018 by April 15, 2019.

Conversion Rules

There are no longer modified AGI limits or filing status requirements relating to rollovers from eligible retirement plans into Roth IRAs.

Conversion contribution. Money distributed from a qualified plan or IRA and reinvested within 60 days into a Roth IRA is called a conversion contribution. The distribution is taxable to the extent it does not represent a return of nondeductible basis. A conversion contribution is not subject to the 10% early withdrawal penalty. A conversion contribution can also be accomplished through a trustee-to-trustee transfer or a same trustee transfer where the trustee simply redesignates a traditional IRA as a Roth IRA rather than open up a new account or issue a new contract.

Income. In the year of conversion, the amount of the distribution from a traditional IRA or employer plan converted to a Roth IRA is included in gross income.

Employer plan conversions. Money in an employer-sponsored retirement plan, such as a 401(k), annuity, section 403(b) plan, government deferred compensation (section 457 plan), or profit-sharing plan, may be directly converted to a Roth IRA.

Inherited IRA. An inherited traditional IRA from someone other than a spouse cannot be converted into a Roth IRA.

Qualified Distributions

A nontaxable qualified distribution is any payment or distribution from a Roth IRA that meets the following requirements.

- 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*
- The payment or distribution is:
  - Made on or after the date you reach age 59½, or
  - Made because you are disabled, or
  - Made to a beneficiary or to your estate after your death, or
  - Made to purchase a first home (up to a $10,000 lifetime limit).

Additional tax on early distributions. If you receive a nonqualified distribution, you must pay the 10% additional tax on early withdrawals penalty on the taxable part of any distributions. Exceptions apply.

Nonqualified distributions. A distribution from a Roth IRA that is not qualified may be partly taxable or nontaxable as there is a set order in which contributions and earnings are considered to be distributed from a Roth IRA. The order is as follows:

1) Regular contributions.
2) Conversion and rollover contributions, on a first-in first-out basis.
3) Earnings on contributions.

Distributions from a Roth IRA that are a return of regular contributions are not subject to tax or penalty, no matter when they are withdrawn. Only the portion of the nonqualified distribution allocable to earnings may be subject to tax and the 10% additional tax.

Are Distributions From Roth IRAs Required?

You are not required to take distributions from your Roth IRA at any age. The required minimum distributions (RMD) rules that apply to traditional IRAs do not apply to Roth IRAs while the owner is alive.

Contact Us

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- Sale or purchase of a residence or other real estate.
- Retirement.
- Notice from IRS or other revenue department.
- Divorce or separation.
- Self-employment.
- Charitable contributions of property in excess of $5,000.

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TAX YEAR
2018

Individual Retirement Accounts
Inherited IRAs

Required Minimum Distributions (RMDs)

Taxpayers generally must begin withdrawing money from their IRA or retirement account upon reaching age 70½. The required minimum distribution (RMD) is the minimum amount that must be withdrawn each year.

Taxpayers may withdraw more than the minimum required amount. For a traditional IRA, withdrawals will be included in taxable income except for any part that was already taxed or that can be received tax-free, such as amounts from a Roth IRA.

Calculating the RMD. The RMD for each year equals the IRA account balance as of December 31 of the preceding year, divided by the applicable distribution period, or life expectancy, for the taxpayer's age in the current tax year.

Year of death. The RMD is calculated using rules for lifetime distributions as if the owner had lived the full year. If the owner died before the required beginning date for distributions, no distribution is required for the year of death.

Inherited Traditional IRAs

Inherited IRA choices. A designated beneficiary has several choices when inheriting a traditional IRA.

1) The beneficiary can cash in the IRA, include the amount in gross income, and pay tax on the distribution.
2) If the beneficiary is an individual, the beneficiary can elect to take the entire account balance in the IRA by the end of the fifth year following the year of the participant's death. No distributions need to be made before the end of the fifth year. This election is available only when the participant dies before the required beginning date for RMD.
3) The beneficiary can leave the IRA in the name of the deceased participant. RMD is determined as follows.
   - If the decedent was already receiving RMDs at the time of death, the beneficiary can take distributions over the longer of:
     - The beneficiary's own life expectancy based on IRS tables, using the age of the beneficiary as of his or her birthday in the year following the year of the decedent's death, reduced by one for each subsequent year, or
     - The decedent's life expectancy based on IRS tables, using the age of the decedent as of his or her birthday in the year of death, reduced by one for each subsequent year.
   - If the decedent was not yet receiving RMDs at the time of death, the beneficiary must take out the distributions over his or her own life expectancy. If the beneficiary was the surviving spouse, RMDs do not begin until the decedent would have turned age 70½.
4) If the beneficiary is the surviving spouse of the deceased IRA participant, the beneficiary can treat the IRA as his or her own. This allows the beneficiary to make additional contributions to the IRA (including rollover contributions). It also allows the beneficiary to use RMD rules based on the beneficiary's life. Early withdrawal penalty rules apply if the surviving spouse is under age 59½.
5) If the beneficiary is the surviving spouse of the deceased IRA participant, the beneficiary can treat the IRA as his or her own by rolling it over to his or her own IRA, or the taxable portion of the IRA can be rolled over to his or her employer-sponsored plan.

Choices 1, 2, and 3 apply to all beneficiaries. Choices 4 and 5 apply only to beneficiaries who are the spouse of the participant.

Individual
Retirement Accounts

Inherited IRAs

10% early withdrawal penalty. The 10% penalty for withdrawal before age 59½ does not apply to a distribution to a beneficiary on or after the death of the participant. However, if a spouse chooses to roll the decedent's IRA into his or her own separate IRA, any subsequent distribution will be subject to the 10% early withdrawal penalty assuming no other exception to the penalty applies.

IRA with basis. Any nondeductible contributions that gave the IRA a basis stay with the IRA after it is inherited by a beneficiary. The basis cannot be combined with the beneficiary's basis in his or her own IRAs unless the beneficiary is the decedent's spouse and chooses to treat the IRA as his or her own.

Inherited Roth IRA

When a Roth IRA owner dies, the minimum distribution rules that apply to traditional IRAs apply to Roth IRAs as though the Roth IRA owner died before his or her required beginning date.

Distributions to beneficiaries. Generally, the entire interest in the Roth IRA must be distributed by the end of the fifth calendar year after the year of the owner's death unless distributions are spread over the life expectancy of the designated beneficiary using the RMD rules. If distributed over the beneficiary's life expectancy the distributions must begin before the end of the calendar year following the year of death. Distributions from another Roth IRA cannot be substituted for these distributions unless the other Roth IRA was inherited from the same decedent. If the sole beneficiary is the spouse, he or she can either delay distributions until the decedent would have reached age 70½ or treat the Roth IRA as his or her own.

Combining with other Roth IRAs. A beneficiary can combine an inherited Roth IRA with another Roth IRA maintained by the beneficiary only if the beneficiary either:

- Inherited the other Roth IRA from the same decedent, or
- Was the spouse of the decedent and the sole beneficiary of the Roth IRA and elects to treat it as his or her own IRA.

Distributions that are not qualified distributions. If a distribution to a beneficiary is not a qualified distribution, it is generally includible in the beneficiary's gross income in the same manner as it would have been included in the owner's income had it been distributed to the IRA owner when he or she was alive. If the owner of a Roth IRA dies before the end of one of the following, the ordering rules for Roth IRA distributions determines which part may be taxable.

- The 5-year period beginning with the first taxable year for which a contribution was made to a Roth IRA set up for the owner's benefit, or
- The 5-year period starting with the year of a conversion contribution from a traditional IRA or a rollover from a qualified retirement plan to a Roth IRA,

Designated Beneficiary Not Determined

If the IRA does not have a designated beneficiary as of the date of death, or the designated beneficiary disclaims his or her interest in the IRA, then the estate can designate one of the estate beneficiaries as the IRA designated beneficiary. The time limit for making this designation is September 30 of the year following the year of the IRA participant's death. By making this designation, the estate can avoid having the IRA distributed under the 5-year rule.

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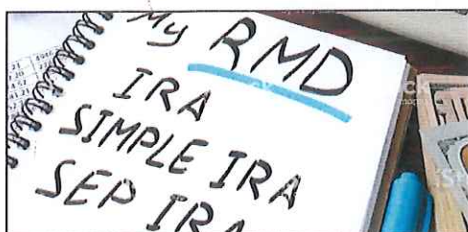

Individual Retirement Accounts
Required Minimum Distributions (RMDs)

Required Minimum Distributions (RMDs)	
IRAs including SEP, SIMPLE and SARSEP IRAs	***Defined Contribution Plans (e.g. 401(k), profit-sharing, and 403(b) plans)***
When do I take my first RMD (the required beginning date)?	
You must take your first RMD by April 1 of the year following the year in which you turn 70½, regardless of whether you are still employed.	April 1 of the year following the later of the year you turn 70 ½ or the year you retire (if allowed by your plan). If you are a 5% owner, you must start RMDs by April 1 of the year following the year you turn 70½.
When do I reach age 70½?	
You reach age 70½ on the date that is six calendar months after the date of your 70th birthday. See *Example #1* and *Example #2,* next page.	Same as IRA rule.
What is the deadline for taking subsequent RMDs after the first RMD?	
After the first RMD, you must take subsequent RMDs by December 31 of each year beginning with the calendar year containing your required beginning date. See *Example #3,* next page.	Same as IRA rule.
How do I calculate my RMD?	
Your RMD is generally determined by dividing the adjusted market value of your IRAs as of December 31 of the preceding year by the distribution period that corresponds with your age in the Uniform Lifetime Table. See *Uniform Lifetime Table* and *Joint Life and Last Survivor Expectancy Table,* next page. If your spouse is your sole beneficiary and is more than 10 years younger than you, you will use the Joint Life and Last Survivor Expectancy Table.	Same as IRA rule. Your plan sponsor/ administrator should calculate the RMD for you.

Required Minimum Distributions (RMDs) continued	
IRAs including SEP, SIMPLE and SARSEP IRAs	***Defined Contribution Plans***
How should I take my RMDs if I have multiple accounts?	
If you have more than one IRA, you must calculate the RMD for each IRA separately each year. However, you may aggregate your RMD amounts for all of your IRAs and withdraw the total from one IRA or a portion from each of your IRAs. You do not have to take a separate RMD from each IRA.	If you have more than one defined contribution plan, you must calculate and satisfy your RMDs separately for each plan and withdraw that amount from that plan. ***Exception:*** If you have more than one 403(b) tax-sheltered annuity account, you can total the RMDs and then take them from any one (or more) of the tax-sheltered annuities.
May I withdraw more than the RMD?	
Yes, an IRA owner can always withdraw more than the RMD. You cannot apply excess withdrawals toward future years' RMDs.	Same as IRA rule.
May I take more than one withdrawal in a year to meet my RMD?	
You may withdraw your annual RMD in any number of distributions throughout the year, as long as you withdraw the total annual minimum amount by December 31 (or April 1 if it is for your first RMD).	Same as IRA rule.
What happens if I do not take the RMD?	
If the distributions to you in any year are less than the RMD for that year, you are subject to an additional tax equal to 50% of the undistributed RMD.	Same as IRA rule.

Individual Retirement Accounts

Required Minimum Distributions (RMDs)

Example #1: *Your 70th birthday was June 30, 2018. You reached age 70½ on December 30, 2018. You must take your first RMD (for 2018) by April 1, 2019.*

Example #2: *Your 70th birthday was July 1, 2018. You reached age 70½ on January 1, 2019. You do not have an RMD for 2018. You must take your first RMD (for 2019) by April 1, 2020.*

Example #3: *You turn 70½ on July 15, 2018. You must take your first RMD, for 2018, by April 1, 2019. You must take your second RMD, for 2019, by December 31, 2019 and your third RMD, for 2020, by December 31, 2020.*

Uniform Lifetime Table

Age	*Distribution Period*	*Age*	*Distribution Period*	*Age*	*Distribution Period*
70	27.4	81	17.9	91	10.8
71	26.5	82	17.1	92	10.2
72	25.6	83	16.3	93	9.6
73	24.7	84	15.5	94	9.1
74	23.8	85	14.8	95	8.6
75	22.9	86	14.1	96	8.1
76	22.0	87	13.4	97	7.6
77	21.2	88	12.7	98	7.1
78	20.3	89	12.0	99	6.7
79	19.5	90	11.4	100	6.3
80	18.7				

For ages not listed in this table, see IRS Pub. 590-B for the complete table.

Joint Life and Last Survivor Expectancy Table

Age	40	41	42	43	44	45	46	47	48	49
70	44.0	43.1	42.2	41.3	40.3	39.4	38.6	37.7	36.8	35.9
71	44.0	43.0	42.1	41.2	40.3	39.4	38.5	37.6	36.7	35.9
72	43.9	43.0	42.1	41.1	40.2	39.3	38.4	37.5	36.6	35.8
73	43.9	43.0	42.0	41.1	40.2	39.3	38.4	37.5	36.6	35.7
74	43.9	42.9	42.0	41.1	40.1	39.2	38.3	37.4	36.5	35.6
75	43.8	42.9	42.0	41.0	40.1	39.2	38.3	37.4	36.5	35.6
76	43.8	42.9	41.9	41.0	40.1	39.1	38.2	37.3	36.4	35.5
77	43.8	42.9	41.9	41.0	40.0	39.1	38.2	37.3	36.4	35.5
78	43.8	42.8	41.9	40.9	40.0	39.1	38.2	37.2	36.3	35.4
79	43.8	42.8	41.9	40.9	40.0	39.1	38.1	37.2	36.3	35.4
80	43.7	42.8	41.8	40.9	40.0	39.0	38.1	37.2	36.3	35.4

Age	50	51	52	53	54	55	56	57	58	59
70	35.1	34.3	33.4	32.6	31.8	31.1	30.3	29.5	28.8	28.1
71	35.0	34.2	33.3	32.5	31.7	30.9	30.1	29.4	28.6	27.9
72	34.9	34.1	33.2	32.4	31.6	30.8	30.0	29.2	28.4	27.7
73	34.8	34.0	33.1	32.3	31.5	30.6	29.8	29.1	28.3	27.5

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Joint Life and Last Survivor Expectancy Table continued

Age	50	51	52	53	54	55	56	57	58	59
74	34.8	33.9	33.0	32.2	31.4	30.5	29.7	28.9	28.1	27.4
75	34.7	33.8	33.0	32.1	31.3	30.4	29.6	28.8	28.0	27.2
76	34.6	33.8	32.9	32.0	31.2	30.3	29.5	28.7	27.9	27.1
77	34.6	33.7	32.8	32.0	31.1	30.3	29.4	28.6	27.8	27.0
78	34.5	33.6	32.8	31.9	31.0	30.2	29.3	28.5	27.7	26.9
79	34.5	33.6	32.7	31.8	31.0	30.1	29.3	28.4	27.6	26.8
80	34.5	33.6	32.7	31.8	30.9	30.1	29.2	28.4	27.5	26.7
81	34.4	33.5	32.6	31.8	30.9	30.0	29.2	28.3	27.5	26.6
82	34.4	33.5	32.6	31.7	30.8	30.0	29.1	28.3	27.4	26.6
83	34.4	33.5	32.6	31.7	30.8	29.9	29.1	28.2	27.4	26.5
84	34.3	33.4	32.5	31.7	30.8	29.9	29.0	28.2	27.3	26.5
85	34.3	33.4	32.5	31.6	30.7	29.9	29.0	28.1	27.3	26.4

Age	60	61	62	63	64	65	66	67	68	69
70	27.4	26.7	26.1	25.4	24.8	24.3	23.7	23.2	22.7	22.2
71	27.2	26.5	25.8	25.2	24.5	23.9	23.4	22.8	22.3	21.8
72	27.0	26.3	25.6	24.9	24.3	23.7	23.1	22.5	22.0	21.4
73	26.8	26.1	25.4	24.7	24.0	23.4	22.8	22.2	21.6	21.1
74	26.6	25.9	25.2	24.5	23.8	23.1	22.5	21.9	21.3	20.8
75	26.5	25.7	25.0	24.3	23.6	22.9	22.3	21.6	21.0	20.5
76	26.3	25.6	24.8	24.1	23.4	22.7	22.0	21.4	20.8	20.2
77	26.2	25.4	24.7	23.9	23.2	22.5	21.8	21.2	20.6	19.9
78	26.1	25.3	24.6	23.8	23.1	22.4	21.7	21.0	20.3	19.7
79	26.0	25.2	24.4	23.7	22.9	22.2	21.5	20.8	20.1	19.5
80	25.9	25.1	24.3	23.6	22.8	22.1	21.3	20.6	20.0	19.3
81	25.8	25.0	24.2	23.4	22.7	21.9	21.2	20.5	19.8	19.1
82	25.8	24.9	24.1	23.4	22.6	21.8	21.1	20.4	19.7	19.0
83	25.7	24.9	24.1	23.3	22.5	21.7	21.0	20.2	19.5	18.8
84	25.6	24.8	24.0	23.2	22.4	21.6	20.9	20.1	19.4	18.7
85	25.6	24.8	23.9	23.1	22.3	21.6	20.8	20.1	19.3	18.6

Age	70	71	72	73	74	75
80	18.7	18.1	17.5	16.9	16.4	15.9
81	18.5	17.9	17.3	16.7	16.2	15.6
82	18.3	17.7	17.1	16.5	15.9	15.4
83	18.2	17.5	16.9	16.3	15.7	15.2
84	18.0	17.4	16.7	16.1	15.5	15.0
85	17.9	17.3	16.6	16.0	15.4	14.8

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- Notice from IRS or other revenue department.
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- Charitable contributions of property in excess of $5,000.

Individual Retirement Accounts
Qualified Charitable Distribution (QCD)

Qualified Charitable Distribution (QCD)

In general, distributions from a traditional IRA are taxable in the year received. However, a qualified charitable distribution (QCD) is generally a nontaxable distribution made directly by the trustee of your traditional IRA (other than a SEP or SIMPLE IRA) to an eligible charitable organization. If all of the qualifications are met, a QCD is nontaxable and you cannot claim a charitable contribution deduction for it. For individuals who do not itemize, taking a QCD can help lower taxable income.

Qualifications and Rules

Certain qualifications must be met:

- You must be at least age 70½ when the distribution is made.
- The maximum annual exclusion for QCDs is $100,000. Any QCD in excess of the $100,000 exclusion limit is included in income as any other distribution. If you file a joint return, your spouse can also have a QCD and exclude up to $100,000.
- All or part of your required minimum distribution (RMD) may be included in the QCD.
- You must have the same type of acknowledgment of your contribution that you would need to claim a deduction for a charitable contribution.
- A charitable contribution deduction on Schedule A (Form 1040), *Itemized Deductions*, cannot be claimed for any QCD not included in income.
- The QCD amount is limited to the amount of the IRA distribution that would otherwise be included in income. If your IRA includes nondeductible contributions, the distribution is first considered to be paid out of otherwise taxable income.

Example: *On December 23, 2018, Jeff, age 75, directed the trustee of his IRA to make a distribution of $70,000 directly to a qualified charitable organization. The total value of Jeff's IRA is $100,000 and consists of $60,000 of deductible contributions and earnings and $40,000 of nondeductible contributions (basis).*

Since Jeff is at least age 70½ and the distribution is made directly by the trustee to a qualified organization, the part of the distribution that would otherwise be includible in Jeff's income is a QCD.

In this case, Jeff has made a QCD of $60,000 (his deductible contributions and earnings).

Jeff includes the total distribution ($70,000) on line 4a of Form 1040. Jeff enters -0- on line 4b. This is Jeff's only IRA and he took no other distributions in 2018.

He also enters "QCD" next to line 4b to indicate a qualified charitable distribution. After the distribution, his basis in his IRA is $30,000.

In 2018, Jeff itemizes his deductions and files Schedule A (Form 1040), deducting the $10,000 portion of the distribution attributable to the nondeductible contributions as a charitable contribution. He cannot take the charitable contribution deduction for the $60,000 portion of the distribution that was not included in his income.

Example: *Janet is single, age 73, and wants to contribute $5,000 to a qualified charity. There are two options available to her:*

- *Make the donation through a QCD, or*
- *Withdraw-then-donate the funds directly to the charity.*

With either option, the $5,000 would count toward meeting her RMD.

Individual Retirement Accounts

Qualified Charitable Distribution (QCD)

Qualified charitable distribution. Janet could make the $5,000 contribution through a QCD by instructing the IRA custodian to send the charity $5,000 directly from her IRA. The QCD does not increase her AGI (or count as income when determining the taxability of her Social Security benefits), and she is not able to claim a charitable contribution deduction for it.

Withdraw-then-donate. Alternatively, she can withdraw $5,000 from her IRA, deposit the funds into her bank account, and then directly make the contribution to the charity. The $5,000 distribution increases her adjusted gross income and *(if she itemizes)* increases her total itemized deductions by the $5,000 charitable contribution. In this instance, the withdraw-then-donate option may be as tax-efficient as the QCD option. However, with the increased standard deduction beginning in 2018, many individuals may no longer itemize their deductions.

In fact, suppose Janet has $9,600 in other itemized deductions. If not for the $5,000 charitable contribution, Jane would use the standard deduction of $13,600 (2018) for a single taxpayer over age 65. With this contribution, she itemizes and deducts $14,600 ($9,600 + $5,000), $1,000 more than the $13,600 standard deduction amount. In this case, she only benefits from $1,000 of the $5,000 contribution. All else being equal, Janet's taxable income would be $4,000 higher with the withdraw-then-donate option than with utilizing a QCD. Janet would need to have $13,600 in other deductions, an amount equivalent to her standard deduction, to make this option match the tax effectiveness of a QCD.

Increase in AGI. Under the withdraw-then-donate option, a taxpayer's AGI will be higher than with the QCD option. A higher AGI could increase taxable income, total tax, and affect various limitations.

- **Social Security.** An increased AGI increases provisional income by the same amount. Provisional income is used to calculate the taxable portion of Social Security benefits. For most Single taxpayers, provisional income between $25,000 and $34,000 causes up to 50% of Social Security benefits to be taxed. Above $34,000 causes up to 85% of Social Security benefits to be taxed, which is the maximum amount that can be taxed. The threshold levels for MFJ are $32,000 and $44,000, but the same principle applies.
- **Capital gains.** An increase in taxable income could push a taxpayer into a higher maximum capital gains tax rate. For 2018, capital gains are taxed at 0% for Single taxpayers with taxable income less than $38,601.
- **Medicare Parts B and D premiums.** The amount of Medicare Part B and Part D premiums are tied to the taxpayer's previous two years' modified AGI. MAGI for 2018 will affect the amount of 2020 premiums.
- **Medical and dental expense deduction limitation.** Medical and dental itemized deductions are limited to the amount that exceeds 7.5% (2018) of AGI. The QCD option could produce a lower total tax bill by setting a lower threshold for deducting medical expenses.
- **Charitable gift deduction limitation.** Gifts donated through a QCD are not reported as itemized deductions or subject to limitation. However, the maximum deduction for cash gifts on Schedule A (Form 1040) is limited to 60% of AGI. Unused portions can be carried forward up to five years.
- **Tax credits limitation.** Many tax credits are limited to taxpayers with AGIs below certain limits.
- **State income tax.** Many states' income taxes are based on federal AGI. Therefore, a QCD could produce a lower state tax bill.

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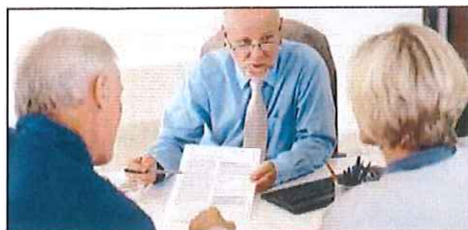

TAX YEAR 2018

Individual Retirement Accounts
Kinds of IRAs and Prohibited Transactions

Kinds of IRAs and Prohibited Transactions

You can open different kinds of IRAs with a variety of organizations. You can open an IRA at a bank or other financial institution or with a mutual fund or life insurance company. You can also open an IRA through your stockbroker. Any IRA must meet Internal Revenue Code requirements, which are listed below for various arrangements.

Traditional IRAs

Your 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.

Individual retirement account. An individual retirement account is a trust or custodial account set up in the United States for the exclusive benefit of you or your beneficiaries. The account is created by a written document. The document must show that the account meets all of the following requirements.

- The trustee or custodian must be a bank, a federally insured credit union, a savings and loan association, or an entity approved by the IRS to act as trustee or custodian.
- The trustee or custodian generally cannot accept contributions of more than the deductible amount for the year. However, rollover contributions and employer contributions to a SEP can be more than this amount.
- Contributions, except for rollover contributions, must be in cash.
- You must have a nonforfeitable right to the amount at all times.
- Money in your account cannot be used to buy a life insurance policy.
- Assets in your account cannot be combined with other property, except in a common trust fund or common investment fund.
- You must start receiving distributions by April 1 of the year following the year in which you reach age 70½.

Individual retirement annuity. You can open 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 your name as the owner, and either you or your beneficiaries who survive you are the only ones who can receive the benefits or payments.

Simplified employee pension (SEP). A SEP is a written arrangement that allows your employer to make deductible contributions to a traditional IRA (a SEP IRA) set up for you to receive such contributions. Generally, distributions from SEP IRAs are subject to the withdrawal and tax rules that apply to traditional IRAs.

A SEP IRA is owned and controlled by the employee, and the employer makes contributions to the financial institution where the SEP IRA is maintained. The employer can decide how much to put into a SEP each year, which gives some flexibility when business conditions vary.

Deemed IRAs. A qualified employer retirement plan can maintain a separate account or annuity under the plan (a deemed IRA) to receive voluntary employee contributions. An employee's account can be treated as a traditional IRA or a Roth IRA. For this purpose, a "qualified employer plan" includes:

- A qualified pension, profit-sharing, or stock bonus plan [section 401(a) plan],
- A qualified employee annuity plan [section 403(a) plan],
- A tax-sheltered annuity plan [section 403(b) plan], and

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- A deferred compensation plan (section 457 plan) maintained by a state, a political subdivision of a state, or an agency or instrumentality of a state or political subdivision of a state.

SIMPLE IRAs

A savings incentive match plan for employees (SIMPLE) plan is a tax-favored written agreement (salary reduction) between you and your employer that allows you to choose to reduce your compensation (salary) by a certain percentage each pay period, and have your employer contribute the salary reductions to a SIMPLE IRA on your behalf.

All contributions under a SIMPLE IRA plan must be made to a SIMPLE IRA, not to any other type of IRA. The SIMPLE IRA can be an individual retirement account or an individual retirement annuity, described above.

If your employer maintains a SIMPLE IRA plan, you must be notified, in writing, that you can choose the financial institution that will serve as trustee for your SIMPLE IRA and that you can roll over or transfer your SIMPLE IRA to another financial institution.

Roth IRAs

A Roth IRA can be either an individual retirement account or individual retirement annuity, described above. To be a Roth IRA, the account or annuity must be designated as a Roth IRA when it is opened. A SEP IRA or SIMPLE IRA cannot be designated as a Roth IRA.

Designated Roth accounts. Designated Roth accounts are separate accounts under 401(k), 403(b), or 457(b) plans that accept elective deferrals that are referred to as Roth contributions. These elective deferrals are included in your income, but qualified distributions from these accounts are not included in your income. Designated Roth accounts are not IRAs and should not be confused with Roth IRAs. Contributions, up to their respective limits, can be made to Roth IRAs and designated Roth accounts according to your eligibility to participate. A contribution to one does not impact your eligibility to contribute to the other.

Prohibited Transactions

Generally, a prohibited transaction is any improper use of your IRA account or annuity by you, your beneficiary, or any disqualified person.

Disqualified persons include your fiduciary and members of your family (spouse, ancestor, lineal descendant, and any spouse of a lineal descendant). The following are some examples of prohibited transactions with an IRA.

- Borrowing money from it.
- Selling property to it.
- Using it as security for a loan.
- Buying property for personal use (present or future) with IRA funds.

Fiduciary. For these purposes, a fiduciary includes anyone who does any of the following.

- Exercises any discretionary authority or discretionary control in managing your IRA or exercises any authority or control in managing or disposing of its assets.
- Provides investment advice to your IRA for a fee, or has any authority or responsibility to do so.
- Has any discretionary authority or discretionary responsibility in administering your IRA.

Effect on an IRA account. Generally, if you or your beneficiary engages in a prohibited transaction in connection with your traditional IRA account at any time during the year, the account stops being an IRA as of the first day of that year and the account is treated as distributing all its assets to you at their fair market values on the first day of the year. If the total of those values is more than your basis in the IRA, you will have a taxable gain that is includible in your income. The distribution may be subject to additional taxes or penalties.

Contact Us

There are many events that occur during the year that can affect your tax situation. Preparation of your tax return involves summarizing transactions and events that occurred during the prior year. In most situations, treatment is firmly established at the time the transaction occurs. However, negative tax effects can be avoided by proper planning. Please contact us in advance if you have questions about the tax effects of a transaction or event, including the following:

- Pension or IRA distributions.
- Significant change in income or deductions.
- Job change.
- Marriage.
- Attainment of age 59½ or 70½.
- Sale or purchase of a business.
- Sale or purchase of a residence or other real estate.
- Retirement.
- Notice from IRS or other revenue department.
- Divorce or separation.
- Self-employment.
- Charitable contributions of property in excess of $5,000.

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Education Tax Benefits

Education Tax Benefits

If you pay tuition, fees, and other costs for attendance at an eligible educational institution for yourself, your spouse, or your dependent, you may be able to take advantage of one or more of the education tax benefits.

You can claim more than one education benefit in a tax year as long as you do not use the same expenses for more than one benefit.

Exception: Qualified expenses used to claim education benefits can also be used to eliminate the 10% penalty on premature IRA distributions.

For each student, you can elect for any year only one of the credits. For example, if you elect to claim the American Opportunity Credit for the student in 2018, you cannot use that same student's qualified education expenses to figure the Lifetime Learning Credit for 2018.

Education Deductions.

Deductions reduce the amount of income subject to income tax. Deductions for education expenses include:

- Student loan interest deduction up to $2,500 from gross income. Income limitations apply.
- Business deduction on Schedule C or F. You can deduct the cost of education related to the business or farm activity.

Education Tax Credits

Tax credits reduce the amount of income tax you may have to pay. Income limitations apply. The education credits are claimed on Form 8863, *Education Credits* (American Opportunity and Lifetime Learning Credits).

- American Opportunity Credit, $2,500 maximum per student per year.
- Lifetime Learning Credit, $2,000 maximum per tax return per year.

Penalty-Free IRA Distributions

If you withdraw money from your IRA before you are age 59½, you are generally subject to a penalty of 10% of the distribution, in addition to any tax that may be due on the distribution.

- The 10% penalty does not apply to traditional IRA or Roth IRA withdrawals, if you use the money to pay qualified education expenses for yourself, spouse, or for any child or grandchild of yourself or your spouse.
- Qualified education expenses include tuition, fees, books, supplies, equipment, and special needs services required for enrollment or attendance at an eligible educational institution. Room and board for students enrolled at least half-time in a degree or certificate program may also qualify.
- Reduce qualified expenses by scholarships and other tax-free assistance the student receives, but not by gifts or inheritances.

Education Tax Benefits

Comparison of Education Credits

American Opportunity Credit	*Lifetime Learning Credit*
Up to $2,500 per eligible student.	Up to $2,000 per tax return.
100% of the first $2,000, plus 25% of the next $2,000 of qualifying expenses for each student.	20% of the first $10,000 of total qualifying expenses.
40% of the credit (up to $1,000) may be refundable.	Nonrefundable tax credit.
Eligible years: • Until the first four years of postsecondary education are completed. • Reduced by number of years the American Opportunity Credit and Hope Credit was claimed for the student.	Eligible years: • All years of postsecondary education.
Qualifying expenses: • Tuition, required enrollment fees, and • Course-related books, supplies, and equipment.	Qualifying expenses: • Tuition and required enrollment fees.
The student must be pursuing an undergraduate degree or other recognized education credential.	The student need not be pursuing a degree or credential.
Student must be enrolled at least half-time for at least one academic period beginning during the year.	Student must be enrolled in at least one course.
Additional restrictions: • The student can have no felony convictions. • Taxpayer cannot use MFS status and cannot be claimed as a dependent by another person. • Additional conditions apply for nonresident aliens and for taxpayers under age 24.	Additional restrictions: • None.

Education Savings Plans

Contributions that you make to education savings plans are not deductible, but the earnings accumulate tax free. In addition, no tax will be owed on distributions if they are less than the beneficiary's qualified education expenses. Qualified expenses are reduced by scholarships, other tax-free assistance, and amounts used to figure education credits.

- ***Qualified Tuition Programs (QTPs).*** States sponsor QTPs to allow prepayment of a student's qualified higher education expenses. For information on a specific QTP, you need to contact the state agency or eligible educational institution that established and maintains it. Effective January 1, 2018, 529 Plans may distribute not more than $10,000 in expenses for tuition during the taxable year for a public, private, or religious elementary or secondary school. Distributions in excess of $10,000 are subject to tax. This limitation applies on a per-student basis, rather than a per-account basis. ***Note:*** QTPs are also called 529 Plans because they are authorized under section 529 of the Internal Revenue Code.
- ***Coverdell Education Savings Accounts (ESAs).*** A Coverdell ESA can be used to pay a student's eligible K-12 expenses, as well as higher education expenses. Coverdell ESA contributions are limited to $2,000 total per year for each beneficiary, no matter how many accounts have been established or how many people are contributing. Unless the beneficiary is a person with special needs, contributions to a Coverdell ESA must stop before the beneficiary reaches age 18 and the account balance must be distributed within 30 days after the beneficiary reaches age 30 (or dies, if earlier).

Exclusions From Gross Income.

An exclusion from income means you don't report the benefit you receive as income and you don't pay tax on it, but you also can't use that same tax-free benefit for a deduction or credit.

- You may exclude the part of scholarships, fellowships, and grants that you use for qualifying education expenses while you are a degree candidate.
- You may exclude up to $5,250 paid for you under a qualifying educational assistance plan. Additional amounts are included in your W-2 income, unless they are a working condition fringe benefit. A working condition fringe benefit is an amount that you could have deducted as an employee business expense, had you paid for it instead of your employer.
- If you cash in qualified U.S. Savings Bonds to pay for eligible education expenses for yourself, spouse, or your dependent, you may exclude the bond interest from income. Income limitations apply.

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