Can I contribute to an IRA?

Tax Letter No. 7 (Rev. 01/2010)

This letter is for informational purposes only and should not be construed as tax advice. Should you have any further questions, we encourage you to contact your tax advisor.

This letter was developed to provide you with information about traditional Individual Retirement Arrangements (IRAs) and to explain how your IMRF participation impacts your IRA deduction. For 2009 there are limits on when you can make a deductible contribution to an IRA.

Federal legislation has also created Roth and Educational IRAs (see page 2). We hope this letter will provide you with the information you need to decide whether to make an IRA contribution and how to handle reporting a contribution when filing your federal tax return.

How much can I contribute?

The Internal Revenue Code allows annual contributions to an IRA up to a maximum of $5,000 ($6,000 **if over age 50**). To make a $5,000 contribution you must have at least $5,000 of taxable compensation. A spouse may also make a $5,000* IRA contribution, provided he or she:

- Has taxable compensation equal to or greater than the IRA contribution

  or

- Files a joint return where the taxable compensation is greater than the IRA contribution for both the member and the spouse

At the same time, the Code has additional rules which determine whether you or your spouse can deduct the IRA contributions from your taxable income. The **additional rules** (page 3) apply when a taxpayer is covered by a pension plan such as IMRF.

Members (and spouses) who are not allowed to deduct an IRA contribution may still make a non-deductible IRA contribution, to either a traditional or Roth IRA, with the same $5,000* limit as a deductible IRA. Like the deductible IRA, the money grows tax-deferred.

When am I covered by a pension plan?

As a member of IMRF, you were covered by a pension plan as of the first date that you started to work in a position that met your employer's hourly standard (600 or 1,000 hours a year). The IRS considers you to be covered by a pension plan even if you are not vested (you do not have eight or more years of IMRF service). At the end of the year, your employer will send you and the IRS a W-2 stating that you are covered by a pension plan.

**$6,000 if over age 50*

Record keeping

If you make non-deductible contributions to a traditional IRA, you need to complete IRS Form 8606. This form details the deductible and non-deductible money in your IRA so you will not pay tax on the withdrawal of non-deductible contributions. However, each withdrawal you make will include at least a proportionate amount of earnings on those contributions that will be taxable.

Roth IRA

The Roth IRA was created by federal legislation (for tax years 1998 and later). Some features of the Roth IRA are:

- The contributions to this IRA are not deductible.

- Earnings in the account are never taxed, if they are withdrawn after you reach age 59-1/2 and the account has been in existence for at least five years.

- IRA contributions are limited to a total of $5,000 ($6,000 **if over age 50**) per year, regardless of the type (traditional or Roth) of IRA or the combination of your contributions. In other words, your total contributions to any combination of IRAs cannot exceed $5,000* per year.

- You can make a $5,000* contribution to a Roth IRA if your adjusted gross income is:

  - below $166,000 for married filing jointly, OR
    (NOTE: for tax year 2010 this amount will increase to $167,000)
  - below $105,000 ($106,000 for 2010) for single taxpayers.
    (NOTE: for tax year 2010 this amount will increase to $106,000)

  The contribution phases out between $166,000 and $176,000 for joint returns, between $105,000 and $120,000 for single files, and between $0 and $10,000 for married filing separately.

- Unlike a regular IRA, contributions can be made to a Roth IRA account after you reach age 70-1/2. However, after you reach age 70-1/2, you must have sufficient earned income to continue making contributions.

- There is no minimum withdrawal requirement for taxpayers over age 70-1/2.

**$6,000 if over age 50*

Roth IRA (continued)

- If your adjusted gross income is less than $100,000 (single or married filing jointly), you may roll over money (convert) from an existing IRA into a Roth IRA. Keep in mind that you must pay income tax on untaxed assets you roll over.
  (NOTE: limit of $100,000 adjusted gross income removed for tax year 2010)

- Lump sum payments (for example, separation refunds or lump sum death benefits) from IMRF can be rolled over to the Roth IRA. However, for taxes this is a taxable distribution. It is treated as if the lump sum was rolled over to an IRA and then converted to a Roth IRA. Your adjusted gross income must also be less than $100,000 (limit removed for 2010).

Coverdell Educational Savings Accounts (Formerly "Education IRA")

Another type of IRA created by legislation (for tax years 1998 and later) is the " Coverdell Educational Savings Account." This type of IRA allows you to make a non-deductible contribution of up to $2,000 a year in an IRA account for a child's (under age 18) higher education. Contributions to Coverdell accounts are not deductible but do grow tax-free until withdrawn. To obtain details about Coverdell accounts, we recommend that you consult with your tax advisor or refer to IRS Publication 970.

Additional Information

Because of the options and record keeping requirements, you need to be familiar with IRS rules and forms. For additional information you can request IRS publications at 1-800-TAX-FORM (1-800-829-3676) or consult a tax advisor. An IRS publication that may be helpful is IRS Publication 590, "Individual Retirement Arrangements."

2009 IRA contribution rules

If you are covered by a pension plan, like IMRF, and your adjusted gross income is under $55,000—you may deduct up to $5,000 a year ($6,000 if over age 50) for a contribution to a traditional IRA.

If you are single and your adjusted gross income (AGI) is

Over $55,000 but under $65,000 *(see note below)*—you may contribute up to $5,000* to an IRA but the amount you may take as a deduction is based on a formula. As your adjusted gross income increases, the amount you can deduct on your tax return decreases. Refer to IRS Publication 590.

(NOTE: for tax year 2010 these amounts will change to "over $56,000 but under $66,000")

Over $65,000—you can make only non-deductible contributions.

**$6,000 if over age 50*

If you are married

For the IMRF member, you may make up to a $5,000* contribution to an IRA, however…

If you file jointly:

And your joint adjusted gross income (AGI) is
Under $89,000—the entire IRA contribution is deductible.
Over $89,000 but under $109,000—a portion of the contribution is deductible.
(Refer to IRS Publication 590)
Over $109,000—the IRA contribution is NOT deductible.

If you file separately:

And your adjusted gross income (AGI) is
Between $0 and $10,000—the deduction phases out.
(Refer to IRS Publication 590)
Over $10,000—the IRA contribution is non-deductible.

If your spouse is covered by a pension plan

- the same rules as above apply, based on whether you file separately or jointly.

If your spouse is not covered by a pension plan:

Your spouse can make a $5,000* contribution to an IRA and deduct it provided:

- you file a joint return.
- the combined earned income is equal to or greater than the IRA contribution(s).
- the combined adjusted gross income is less than $166,000. *(NOTE: for tax year 2010 this amount will increase to $167,000)*

***$6,000 if over age 50*