

Traditional IRA

Answers

To Your

Questions

The next best thing to a money tree

Wouldn't it be nice if you could plant a money tree in the backyard, and whenever you needed a little extra cash, you could pick a few bills? The traditional IRA could be the next best thing! With a little patience, and steady contributions, you'll see your IRA grow into an account that will help provide safety and security for you and your family for years to come.

Is the traditional IRA for you? Hopefully, this brochure will help you decide. We have compiled answers to the most commonly asked questions in order to give you a better understanding of the traditional IRA, which is available right here at your credit union. We hope that this information will be valuable when you evaluate your savings options.

Of course, it's important to get all the details before you make your decisions. We are here to help answer your traditional IRA questions.

Q. What is a traditional IRA?

A. A traditional IRA is a type of retirement plan that has been in existence since 1975. Traditional IRAs offer tax-deferred earnings, and the possibility for tax-deductible contributions. These tax advantages make the traditional IRA a powerful tool in creating a balanced, long-term savings plan.

Q. How does the traditional IRA work?

A. You can contribute to a traditional IRA if you earn compensation and you will not reach age 70½ by the end of the year. If you file a joint tax return, you can treat your spouse's compensation as your own (except your combined contributions cannot exceed your combined compensation). All earnings in the traditional IRA are not taxed until they are withdrawn. The ability to defer taxes on the earnings, and to withdraw in a year when you may be in a lower tax bracket, can mean more after-tax dollars for your retirement.

Q. How much can I contribute to a traditional IRA?

A. If you meet the eligibility tests described above and you are under age 50, you can contribute up to \$3,000 for 2002 through 2004. If you have attained age 50 by the end of the year, then your limits are \$3,500 for 2002 through 2004. These limits are even higher for later years.

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

A. Yes, your participation in an employer-sponsored retirement plan will not affect your ability to contribute to a traditional IRA

(assuming age and compensation requirements are met). However, higher-income earners will lose their ability to deduct their traditional IRA contributions if participating in an employer-sponsored plan.

Q. If I already have a Roth IRA, can I have a traditional IRA, too?

A. Yes, you can. However, the limits on annual contributions described on the previous page apply to any combination of traditional and Roth IRA contributions that you make for the year.

Q. How much can I deduct?

A. The table below summarizes the deduction rules. If you are single, or married and neither spouse is an active participant in a retirement plan, your traditional IRA contribution is deductible regardless of income. If you or your

spouse is an active participant, you may deduct contributions only if your income is below certain limits. Smaller deductions are available if your income is within the phase-out range, which is determined by your filing status. Higher income earners with retirement plans may still contribute, but deductions are not available if income is over the phase-out range. If you have questions about your specific tax situation, please consult your tax advisor for an interpretation of how these rules apply to you.

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

A. You may be able to receive a tax credit for making contributions through tax year 2006. The full credit is 50 percent of the first \$2,000 of contributions. The full credit is available for joint filers who have joint modified adjusted gross income (MAGI) up to \$30,000, heads of households with MAGI up to \$22,500, or

	Full Deduction	Smaller Deduction	No Deduction
2002	<ul style="list-style-type: none"> • Single, not an active participant • Single, an active participant, MAGI under \$34,000 • Married, neither spouse an active participant • Joint filer, owner is an active participant, MAGI under \$54,000 • Married, spouse is an active participant, while owner is not, MAGI is under \$150,000 	<ul style="list-style-type: none"> • Single, active participant, MAGI \$34,000-\$44,000 • Joint filer, owner is an active participant, joint MAGI \$54,000-\$64,000 • Married, spouse is an active participant, while owner is not, MAGI is \$150,000-\$160,000 	<ul style="list-style-type: none"> • Single, active participant, MAGI over \$44,000 • Joint filer, owner is an active participant, MAGI over \$64,000 • Married, spouse is an active participant, while owner is not, MAGI is over \$160,000
2003	<ul style="list-style-type: none"> • Single, not an active participant • Single, an active participant, MAGI under \$40,000 • Married, neither spouse an active participant • Joint filer, owner is an active participant, MAGI under \$60,000 • Married, spouse is an active participant, while owner is not, MAGI is under \$150,000 	<ul style="list-style-type: none"> • Single, active participant, MAGI \$40,000-\$50,000 • Joint filer, owner is an active participant, joint MAGI \$60,000-\$70,000 • Married, spouse is an active participant, while owner is not, MAGI is \$150,000-\$160,000 	<ul style="list-style-type: none"> • Single, active participant, MAGI over \$50,000 • Joint filer, owner is an active participant, MAGI over \$70,000 • Married, spouse is an active participant, while owner is not, MAGI is over \$160,000

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.

Q. Will I owe income taxes when I withdraw from my traditional IRA?

A. Yes, you will owe income taxes when you withdraw from your traditional IRA. However, if you make nondeductible contributions to a traditional IRA, a portion of each withdrawal will be treated as the nontaxable return of these contributions.

Q. If I make an early withdrawal from my traditional IRA before age 59½, do I pay a penalty?

A. In general, you must pay a ten percent tax on early distributions or withdrawals before age 59½. But the early distribution tax does not apply in the following situations:

- a) Amount is rolled over or directly transferred to another traditional IRA
- b) Amount is properly converted to a Roth IRA
- c) Withdrawal of an excess contribution before the tax return is due
- d) Withdrawal of an excess contribution after the filing deadline if certain conditions are met
- e) Payment is made to your beneficiaries after your death
- f) Withdrawal of up to \$10,000 is for first-time home purchase
- g) Amount is used to pay for qualified post-secondary education expenses

- h) Amount is used to pay for medical expenses in excess of 7.5% of adjusted gross income (AGI)
- i) Amount is for pre-59½ periodic payments
- j) Distribution is to an owner who is disabled (as defined by the IRS code)
- k) Distribution is for medical insurance premiums during unemployment that lasts 12 weeks or longer

Q. When must I begin taking distributions from my traditional IRA?

A. You must begin taking required minimum distributions from your traditional IRA at age 70½. The minimum distributions each year will be computed using an IRS formula. You are allowed to delay the first year's payment until April 1 of the following year, but you will receive two year's worth of payments in your 71½ year if you choose to delay.

Q. Can I move funds from a qualified retirement plan to a traditional IRA?

A. If you are entitled to receive an eligible rollover distribution from an employer's plan, you can continue deferring taxes by moving the money into a traditional IRA. The best way to do this is to inform the plan administrator that you want the funds moved directly to your traditional IRA in a direct rollover. The plan administrator will inform you before making an eligible rollover distribution.

Q. Can I move money from a traditional IRA to a Roth IRA?

A. You can move money from your traditional IRA to a Roth IRA if your adjusted gross income for the year is \$100,000 or less, and you are either single or married filing a joint tax return. In the year you convert, you will have to pay federal income taxes on the amount that you move, except the portion that is treated as the return of your nondeductible contribution. You may also be subject to state income taxes.

Q. What happens to my traditional IRA after my death?

A. You may designate one or more beneficiaries to receive your IRA after your death. If your spouse is your beneficiary, he or she may directly transfer your traditional IRA to his or her own IRA tax-free. In addition, all beneficiaries have the option of taking a lump-sum payment, and in most cases, they will be able to take periodic payments over a number of years. Any tax-deferred money in your traditional IRA at the time of death will be taxed when it is distributed to your beneficiaries.

Not intended as tax advice. Please consult a tax professional.