Traditional IRAs

Deadline to Establish and Fund an IRA

An IRA can be established and funded at any time from January 1 of the current year and up to and including the date an individual's income tax return is due (generally, April 15 of the following year), not including extensions.

Can Deduction Be Taken Prior to Investing the Funds?

Yes! This, in effect, permits an individual to file his return early in the year (e.g., January) and use his or her tax refund to make the actual contribution prior to April 15. If desired, refunds of federal income taxes may be directly deposited into an IRA.

Types of Arrangements Permitted

There are currently two types of IRAs:

- **Individual retirement accounts:** These are trusts or custodial accounts with a corporate trustee or custodian.
- **Individual retirement annuities:** Special annuities issued by an insurance company.

Contribution and Deduction Limits

A taxpayer may contribute the lesser of $7,500[1] or 100% of compensation[2] for the year. If a taxpayer is married, an additional $7,500 may be contributed on behalf of a lesser earning (or nonworking) spouse, using a "spousal" IRA. Thus, the family could contribute up to $15,000[3] as long as total family compensation is at least that amount. A taxpayer age 50 or older may contribute an additional $1,100 ($2,000 if the spouse is also age 50 or older). The $1,100 additional amount is subject to adjustment for inflation in future years. Contributions may be made at any age, as long as the taxpayer has compensation. If certain requirements are met, the contributions may be deducted from gross income on the federal income tax return.

[1] This amount applies to 2025 and 2026.

[2] "Compensation," generally, includes taxable wages, salaries, commissions, and the net income from self-employment.

[3] This amount applies to 2026.

Participating In Other Retirement Plans May Reduce Deductions

Taxpayers who participate in an employer's plan may make fully-deductible IRA contributions only if their modified adjusted gross income (MAGI)[1] is below $129,000 if married filing jointly, $81,000 if single, and $0 if married filing separately. If MAGI exceeds these amounts, the $15,000 family or $7,500 individual maximum is reduced by a formula that eventually permits no deduction. No IRA deduction is allowed for married couples filing jointly with MAGI over $149,000, single individuals with a MAGI over $91,000, and married couples filing separately with an individual MAGI over $10,000[2].

For 2026, a taxpayer who is not an active participant in an employer plan, but whose spouse is, the maximum deductible IRA contribution is phased out if their combined MAGI is between $242,000 and $252,000.

Employer plans include: regular qualified plans; Keogh plans; Sec. 403(b) tax-sheltered annuity plans; simplified employee pension (SEP) plans; SIMPLE plans; and state, federal and local government plans (except Sec. 457 tax-exempt employer sponsored nonqualified deferred compensation plans).

Individuals with income in excess of the above limits may wish to consider contributing to either a traditional IRA or a Roth IRA, on a nondeductible basis. There are income limits applicable to Roth IRA accounts which may prevent a high-income taxpayer from contributing to a Roth IRA.

Distributions, Withdrawals and Taxation

- **Typical distribution plans.**
  - **Single-sum distribution:** Becomes part of taxable income for that year (less any nondeductible contributions).
  - **Life expectancy:** Each year, participant calculates payout based upon the attained-age life expectancy, using life expectancy tables issued by the federal government.

[1] Modified adjusted gross income (MAGI) is a taxpayer's adjusted gross income (AGI) with certain deductions or exclusions added back. For most taxpayers, MAGI and AGI are the same.

[2] These are 2026 limits. For 2025 the phase-out ranges were (1) MFJ - MAGI of $126,000 - $146,000; (2) Single - $79,000 - $89,000. For taxpayers using the MFS filing status, the phase-out range is $0 - $10,000, which does not change.

- **Life annuity:** For individual retirement annuities only, participant/annuitant may elect income for life (and the life of a joint annuitant, if desired).

- **Premature distributions:** Taxable distributions from an IRA before a participant reaches age 59½ are subject to a 10% federal tax penalty for "early" withdrawal. The 10% penalty may not apply if one of a number of exceptions applies (See IRC Sec. 72(t)). All taxable distributions are included in the IRA owner's gross income in the year of distribution.

- **Required minimum distributions (RMDs):** Must begin by April 1 of the year following the year in which the participant reaches age 73[1]. If this initial distribution is received in the year following the year in which the participant reaches age 73, two distributions are required in that year. Thereafter, the RMD must be made by the end of each calendar year. For tax years beginning after December 29, 2022, a 25% excise tax applies to amounts that should have been distributed, but were not. For tax years beginning before December 30, 2022, a 50% excise tax applied. The 25% penalty is further reduced to 10% if the taxpayer submits an amended return reflecting the correct RMD amount, as well as the 10% penalty, within a specified time frame.

The dollar amount of each year's RMD is calculated using one of two life expectancy tables:

  - **Over the life expectancy of the participant:** In general, the required minimum distribution is calculated using the IRA participant's attained age and a minimum distribution factor table prescribed by the IRS, the Uniform Lifetime Table.

  - **Spouse more than 10 years younger:** If the participants' spouse is more than 10 year younger than the participant, and the spouse is the IRA's sole designated beneficiary for the entire calendar year, the minimum distribution factor used in calculating the RMD amount is determined using the Joint and Last Survivor Table. The participant's marital status is determined as of January 1 of the calendar year.

  - **Coronavirus-related distribution (CRD):** One section of the Coronavirus Aid, Relief, and Economic Security (CARES) Act provided for a "Coronavirus-related distribution," or CRD. A CRD – optional (not mandatory) for a qualified retirement

[1] Under current regulations, the age to begin RMDs increases after 2022 to: (1) age 73 for those born from 1951 to 1959; and (2) to age 75 for those born after 1959. Previously, age 72 was the mandated age to begin RMDs.

plan sponsor - was a distribution made from January 1, 2020 through December 30, 2020 from an IRA or qualified retirement plan. A CRD could not exceed $100,000 in aggregate per individual, was exempt from the usual 20% mandatory federal tax withholding, and must have been made to an individual (or spouse or dependent) who was diagnosed with SARS-CoV-2 or COVID-19, or who experienced an adverse financial consequence as a result of the COVID-19 pandemic. A CRD was exempt from any 10% early withdrawal penalty that may have applied and, unless the individual chose otherwise, the CRD will be included in taxable income ratably over a three-year period. A CRD could be re-paid, without regard to the normal contribution limits, over a three-year period.

- **Taxation of distributions.**
  - **During life:** Distributions are taxable as ordinary income.[1]
  - **At death**: At the IRA account owner's death, the distributions received by a beneficiary are generally taxed as ordinary income. A surviving spouse may elect to receive distributions from an inherited IRA over his or her life expectancy. For most non-spouse beneficiaries, IRA balances must be completely distributed over a period of time not to exceed 10 years. In addition to surviving spouses, an exception to the 10-year rule applies to disabled or chronically ill individuals, to someone who is not more than 10 years younger than the IRA owner, or to a minor child of the IRA owner. Once a minor child reaches age 21, the requirement to completely distribute any remaining balance in the IRA over no more than 10 years applies.[2]
  - **Qualified charitable distribution (QCD)**: Federal income tax law provides for an exclusion from gross income in 2026 of up to $111,000 ($108,000 in 2025) for distributions made from a Roth or traditional IRA *directly* to a qualified charitable organization. The amount excluded from gross income may be reduced if an individual continues to make deductible IRA contributions after reaching age 70½. If applicable, a QCD counts towards the taxpayer's RMD requirements. The IRA owner (or beneficiary of an inherited IRA) must be at least age 70½ when the distribution is made. No charitable deduction is allowed for a QCD.

[1] Taxes and penalties do not apply to nondeductible contributions.

[2] These distribution requirements generally apply to individuals who die *after* December 31, 2019. A different set of distribution requirements apply to individuals who died *before* January 1, 2020.

For distributions after December 29, 2022, federal tax law also provides for a *one-time* distribution in 2026 of up to $55,000 ($54,000 in 2025) to a charitable gift annuity, a charitable remainder unitrust, or a charitable remainder annuity trust.

Both the $111,000 and $55,000 amounts are subject to adjustment for inflation in future years.

- **Transfers to Health Savings Accounts (HSAs):** Federal law allows for a limited, one-time, direct transfer of funds from an IRA to an HSA. If certain requirements are met, any otherwise taxable portion of the distribution is excluded from income and the 10% early distribution penalty will not apply.

Investment Alternatives

- **Banks, savings and loans, credit unions:** Certificates of deposit in Traditional IRAs are generally protected by either the FDIC or the NCUA for amounts up to $250,000. Fixed and variable rates are available. There may be penalties for early withdrawal.
- **Annuities:** Traditional individual retirement annuities issued by insurance companies can guarantee a fixed monthly income at retirement.[1] Variable annuities do not guarantee a fixed monthly income at retirement.
- **Money market:** Yield fluctuates with the economy. Investor cannot lock in the higher interest rates. It is easy to switch to other investments.
- **Mutual funds and Exchange-Traded Funds (ETFs):** Capital gains, interest and dividends are tax-deferred in an IRA but are taxed as ordinary income at withdrawal.
- **Zero coupon bonds:** Generally purchased at a deep discount from face value, "zeros" are subject to both inflation risk and interest rate risk.
- **Stocks and bonds:** A wide variety of investments and risk is possible. Capital gains are taxed as ordinary income at withdrawal. Losses are generally not deductible.
- **Limited partnerships:** Some limited partnerships are especially designed for qualified plans, specifically in the areas of real estate and mortgage pools.

[1] Annuity guarantees are based on the claims-paying ability of the issuing insurance company.

Prohibited Investments or Transactions for IRAs

- **Life insurance:** IRAs cannot include life insurance contracts.
- **Collectibles:** The purchase of art works, antiques, metals, gems, stamps, etc. will be treated as a taxable distribution. Coins issued under state law and certain U.S. gold, silver, and platinum coins are exceptions; some kinds of bullion may be purchased.
- **Loans to IRA taxpayer:** Self-borrowing disqualifies the IRA and triggers a constructive distribution of the fair market value of the entire amount in the IRA as of the first day of the tax year. Amounts so distributed are included in gross income. This is true whether the IRA is an individual retirement account or an individual retirement annuity. If the owner is under age 59½ at the time of a deemed distribution, a 10% tax penalty for early withdrawal will be added, unless an exception applies.
- **IRA as collateral:** If the owner of an individual retirement account pledges any portion of the account as security for a loan, the portion so pledged is deemed distributed, and included in gross income, as of the first day of the tax year in which the loan is made. If the owner of an individual retirement annuity pledges any portion of the contract as security of a loan, the fair market value of the entire amount in the account is deemed distributed, and included in gross income, as of the first day of the tax year. In both situations, if the owner is under age 59½ at the time of a deemed distribution, a 10% tax penalty for early withdrawal will be added, unless an exception applies.
- **IRA Involved in a Prohibited Transaction:** The Secure 2.0 Act of 2022 clarified that if an IRA engaged in a prohibited transaction, assuming that the IRA owner had more than one IRA, only the IRA in which the prohibited transaction occurred would be disqualified.

Other Factors to Consider

- Is the interest rate fixed or variable? If interest rates drop, a fixed rate is better, especially if you can make future contributions at the same fixed rate. If interest rates go up, you may be able to roll the current IRA over to another IRA.
- What is the yield? More frequent compounding will produce a higher return.
- How often can you change investments? What is the charge?
- Federal bankruptcy law protects assets in traditional IRA accounts, up to $1,711,975.[1] Funds rolled over from qualified plans, however, are protected without limit

[1] Effective April 1, 2022. The limit is indexed for inflation every three years.

Disclosure Notice

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