

Roth IRAs and Retirement Accounts

Get up to speed on individual retirement accounts, from the basics of traditional IRAs to the nuances that set Roth IRAs apart. This updated course walks through eligibility and contribution rules, conversion strategies, and recharacterization mechanics, then dives into distribution rules—covering qualified distributions, early withdrawal penalties, and required minimum distribution considerations. A dedicated chapter on Roth 401(k) plans rounds out the coverage. Perfect for CPAs and tax professionals looking to sharpen their Roth IRA knowledge and deliver more confident, informed guidance to clients.

CREDIT HOURS 2 | FIELD OF STUDY TAXES | EXAM QUESTIONS 10

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LEARNING ASSIGNMENTS AND OBJECTIVES

Assignment

- Study the full course materials included here.
- Complete the review questions after each chapter.
- Answer 10 final exam questions.
- Final exam is scored immediately, 70% or better passes.
- Certificate of completion is available in your account.
- Failed exams can be retaken free of charge.

Course Objectives

- Identify the key characteristics of traditional IRAs.
- Identify the similarities and differences between Roth and traditional IRAs.
- Recall the contribution rules for Roth IRAs.
- Recall the requirements for converting a traditional IRA to a Roth IRA.
- Identify the taxation rules of Roth IRA distributions.
- Recognize the differences between a designated Roth 401(k) account and a Roth IRA.

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Chapter 1: INTRODUCTION TO INDIVIDUAL RETIREMENT ACCOUNTS

Chapter Objective

After completing this chapter, you should be able to:

- Identify the key characteristics of traditional IRAs.

I. TRADITIONAL IRAs

Simply put, a traditional Individual Retirement Account (IRA) is any IRA that is not a Roth IRA or a SIMPLE IRA. You are eligible to establish an IRA if you received taxable compensation during the year. Prior to January 1, 2020, an individual was unable to contribute if they were age 70½ or older. For 2020 and later, there is no age limit on making regular contributions to a traditional IRA.

Individuals are eligible for a traditional IRA whether or not they are covered by any other retirement plan. However, individuals may not be able to deduct all of their contributions if they or their spouse are covered by an employer retirement plan. If both an individual and his or her spouse have compensation, each may establish an IRA. However, spouses cannot participate in the same IRA.

A qualified individual may establish a traditional IRA at any time. However, the time for making contributions for any year is limited. This topic is discussed in more detail below.

A. COMPENSATION

For purposes of being eligible to make an IRA contribution – either Roth or traditional – compensation is what you earn from working. Compensation includes, but is not limited to, the following items.

1. Wages and Salaries

Wages, salaries, tips, professional fees, bonuses, and other amounts you receive for providing personal services are compensation. The IRS treats as compensation any amount properly shown in box 1 (Wages, tips, other compensation) of Form W-2, Wage and Tax Statement, provided that amount is reduced by any amount properly shown in box 11 (Nonqualified plans). A scholarship or fellowship is generally taxable compensation only if it is in box 1 of your Form W-2. However, for tax years beginning after 2019, certain non-tuition fellowship and stipend payments not reported to you on Form W-2 are treated as taxable compensation for IRA purposes. These amounts include taxable

non-tuition fellowship and stipend payments made to aid you in the pursuit of graduate or postdoctoral study and included in your gross income.

2. Commissions

An amount you receive that is a percentage of profits or sales price is compensation.

3. Self-employment Income

If you are self-employed (a sole proprietor or a partner), compensation is the net earnings from your trade or business (provided your personal services are a material income-producing factor) reduced by the total of:

- The deduction for contributions made on your behalf to retirement plans, and
- The deduction allowed for the deductible part of your self-employment taxes.

Compensation includes earnings from self-employment even if they aren't subject to self-employment tax because of your religious beliefs.

Self-employment loss. If you have a net loss from self-employment, don't subtract the loss from your salaries or wages when figuring your total compensation.

4. Alimony and Separate Maintenance

For IRA purposes, compensation includes any taxable alimony and separate maintenance payments you receive under a decree of divorce or separate maintenance but only with respect to divorce or separation instruments executed on or before December 31, 2018, that have not been modified to exclude such amounts.

5. Nontaxable Combat Pay

If you were a member of the U.S. Armed Forces, compensation includes any nontaxable combat pay you received. This amount should be reported in box 12 of your 2026 Form W-2 with code Q.

6. Graduate or Postdoctoral Study

A scholarship or fellowship is generally taxable compensation only if it is in box 1 of your Form W-2. However, for tax years beginning after 2019, certain non-tuition fellowship and stipend payments not reported to you on Form W-2 are treated as taxable compensation for IRA purposes. These amounts include taxable non-tuition fellowship and stipend payments made to aid you in the pursuit of graduate or postdoctoral study and included in your gross income.

TABLE 1.1 COMPENSATION FOR PURPOSES OF AN IRA

Note. These rules apply to both traditional and Roth IRAs.

Items Considered Compensation	Items Not Considered Compensation
• Wages, salaries, etc.	• Earnings and profits from property
• Commissions	• Interest and dividend income
• Self-employment income	• Pension or annuity income
• Taxable alimony and separate maintenance	• Deferred compensation
• Nontaxable combat pay	• Income from certain partnerships
• Taxable non-tuition fellowship and stipend	• Any amounts excluded from income payments

B. TYPES OF INDIVIDUAL RETIREMENT ACCOUNTS

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. The requirements for the various arrangements are discussed below.

1. 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 can't accept contributions of more than the deductible amount for the contributions to a traditional SEP IRA 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 can't be used to buy a life insurance policy.
- Assets in your account can't 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 73.

2. 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.

An individual retirement annuity must meet all the following requirements.

- Your entire interest in the contract must be nonforfeitable.
- The contract must provide that you can't transfer any portion of it to any person other than the issuer.
- There must be flexible premiums so that if your compensation changes, your payment can also change. This provision applies to contracts issued after November 6, 1978.
- The contract must provide that contributions can't be more than the deductible amount for an IRA for the year, and that you must use any refunded premiums to pay for future premiums or to buy more benefits before the end of the calendar year after the year in which you receive the refund.
- Distributions must begin by April 1 of the year following the year in which you reach age 73.

3. SIMPLE IRA Plans and SIMPLE IRAs

A SIMPLE IRA plan is a tax-favored retirement plan that certain small employers (including self-employed employees) can set up for the benefit of their employees. Contributions to the employees' SIMPLE IRA are made by the employers and are made up of salary reduction contributions and employer contributions which are either matching contributions or nonelective contributions. A SIMPLE IRA can be either a traditional SIMPLE IRA or a Roth SIMPLE IRA but are subject to different rules than traditional or Roth IRAs.

4. Simplified Employee Pension (SEP) Arrangements and SIMPLE IRAs

A SEP arrangement is a written plan that allows an employer to make contributions to an employee's traditional SEP IRA or Roth SEP IRA. Employer contributions to SEP IRAs are subject to different limits than individual contributions to traditional and Roth IRAs. Distributions from SEP IRAs are subject to traditional and Roth IRA rules.

5. Employer and Employee Association Trust Accounts

Your employer or your labor union or other employee association can set up a trust to provide individual retirement accounts for employees or members, provided certain requirements are met (such as separate accounting). The requirements for individual retirement accounts apply to these traditional and Roth IRAs.