

ROTH IRA BASICS



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ADVISORS

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Luke Neff regularly partners with individuals and families to make smart financial decisions through comprehensive financial planning and portfolio management.

He values life-long-learning and has demonstrated this through formal higher education earning a Master of Science in Personal Financial Planning and other Certifications.

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Lisa works with Luke Neff and his clients to provide administrative support. She brings with her 20 plus years of experience in this role.

She is Series 7, 63, and 65 licensed.

INTRODUCTION TO ROTH IRAs

- Contributions are made on an after-tax basis
- There's no up-front tax benefit
- Qualified distributions are entirely free from federal income tax
- Caution: Different rules may apply for state tax purposes



TRADITIONAL IRA VS. ROTH IRA

Traditional IRA

- Can make annual contribution if you have taxable compensation
- Deductible contributions depend on income, filing status, and coverage by retirement plan
- Can make after-tax (nondeductible) contributions
- Distributions subject to federal income tax, except for after-tax contributions
- Distributions prior to age 59½ may be subject to additional 10% penalty tax
- Distributions required after 72
- Funds grow tax deferred

Roth IRA

- Can make annual contribution if you have taxable compensation
- Ability to contribute depends on income level and filing status
- All contributions are after-tax (no up-front deduction)
- Qualified distributions are entirely free from federal income taxes
- For nonqualified distributions, earnings subject to federal income tax and 10% penalty tax may apply if under 59½
- No lifetime required distributions
- Funds grow tax deferred/tax free

ROTH TAX-FREE QUALIFIED DISTRIBUTIONS

Qualified distributions are federal income tax free.

For a distribution to be qualified, it must meet BOTH of the following requirements:

- Satisfy five-year holding period

AND

- Have qualifying event
 - Age 59½
 - Disability
 - First-time homebuyer expenses (limited to \$10,000 lifetime from all IRAs)
 - Death



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ROTH QUALIFIED DISTRIBUTIONS: THE FIVE-YEAR HOLDING PERIOD

- Five-year holding period begins on the first day of tax year for which you first made a contribution (annual, rollover, or conversion) to ANY Roth IRA
- Five-year holding period ends after five calendar years
- Applies to your beneficiaries after your death as well
- Spouse beneficiary can roll over to own Roth IRA or treat your Roth IRA as his or her own. In either case, the five-year holding period begins on the *earlier* of:
 - January 1 of tax year your spouse first established any Roth IRA, or
 - January 1 of tax year you first established any Roth IRA

Period begins on January 1 of first tax year for which you made a contribution to any Roth IRA

- Can make a regular (annual) contribution to an IRA for a tax year until April 15 of following year
- If you make regular contributions to first Roth IRA on April 15, 2021, and designate contribution for 2020, five-year holding period begins on January 1, 2020

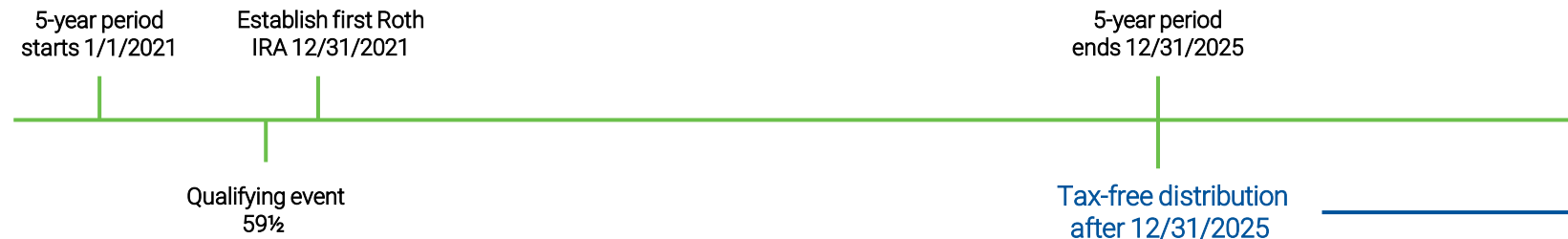


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QUALIFIED DISTRIBUTIONS – EXAMPLE

1

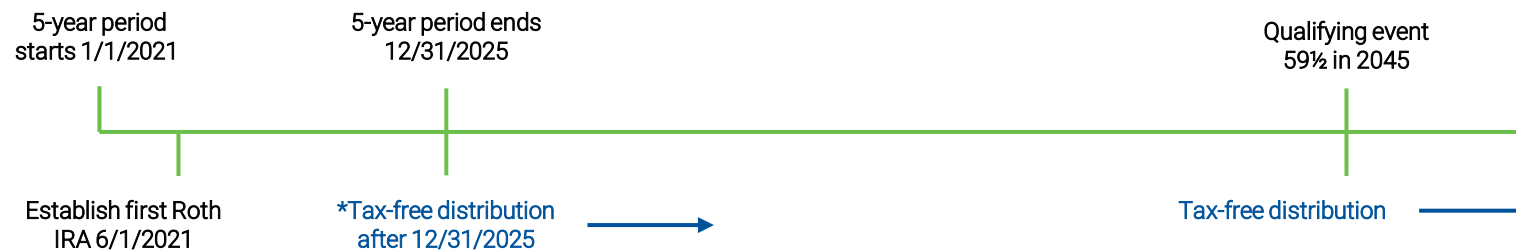
- Age 60
- Establish first Roth IRA on December 31, 2021, by converting a traditional IRA to a Roth IRA
- Must have qualifying event AND satisfy five-year holding period
- Here qualifying event has occurred – you've attained age 59½
- Five-year holding period begins January 1, 2021
- Five-year holding period ends December 31, 2025
- Tax-free qualified withdrawals from this Roth IRA, and any other Roth IRA you own, available anytime after December 31, 2025



QUALIFIED DISTRIBUTIONS – EXAMPLE

2

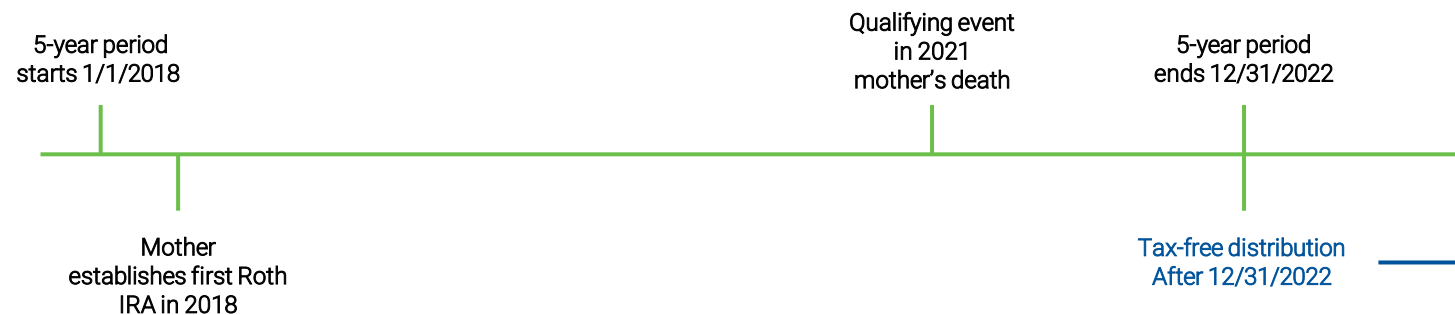
- Age 35
- Establish first Roth IRA on June 1, 2021, by making a rollover from a 401(k) plan to the Roth IRA
- Must have qualifying event AND satisfy five-year holding period
- Here qualifying event has occurred – you’ve attained age 59½
- Five-year holding period begins January 1, 2021
- Five-year holding period ends December 31, 2025
- Tax-free qualified withdrawals available from this Roth IRA, and any other Roth IRA you own:
 - In 2045, after you attain age 59½
 - After December 31, 2025, if you become disabled or die*
 - After December 31, 2025, if you have first-time homebuyer expenses (up to \$10,000 lifetime from all IRAs)*



QUALIFIED DISTRIBUTIONS – EXAMPLE

3

- You inherit a Roth IRA from your mother in 2021
- Your mother established her first Roth IRA in 2018 by making a regular annual contribution
- Must have qualifying event AND satisfy five-year holding period
- Qualifying event is your mother's death
- Five-year holding period begins January 1, 2018
- Five-year holding period ends December 31, 2022
- Tax-free qualified withdrawals are available from the inherited Roth IRA anytime after December 31, 2022



NONQUALIFIED ROTH DISTRIBUTIONS

Nonqualified distribution: You haven't satisfied the five-year holding period or you don't have a qualifying event

- Your contributions come out tax free
- Your contributions come out first
- Taxable earnings come out last
- Earnings are subject to income tax, and 10% penalty tax unless exception applies

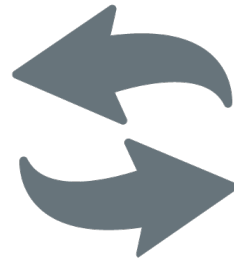


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WAYS TO FUND A ROTH IRA



Regular Annual
Contributions



Convert Traditional IRA
to Roth IRA



Rollover from Eligible
Employer Plan to Roth IRA

FUNDING ANNUAL ROTH CONTRIBUTIONS

- You can continue up to \$6,000 to a Roth IRA in 2021
- Individuals age 50 or older can make additional “catch-up” contribution of \$1,000
- Annual contributions may be limited depending on income level and filing status:

Federal filing status	2021 Roth contribution reduced if MAGI is:	You can't contribute to a Roth IRA in 2021 if your MAGI is:
Single or head of household	More than \$125,000 but less than \$140,000	\$140,000 or more
Married filing jointly or qualifying widow(er)	More than \$198,000 but less than \$208,000	\$208,000 or more
Married filing separately	More than \$0 but less than \$10,000	\$10,000 or more

CONVERTING A TRADITIONAL IRA TO A ROTH IRA

- Taxed in year of conversion as if you took a withdrawal (but 10% early distribution does not apply)
- Trade off immediate taxation for possibility of tax-free qualified distributions in future
- You can also convert SIMPLE IRAs (after two-year waiting period) and SEP-IRAs to Roth IRAs



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WAYS TO CONVERT A TRADITIONAL IRA TO A ROTH IRA

- Rollover
- Trustee-to-trustee transfer
- Same-trustee transfer

CALCULATING THE CONVERSION TAXES

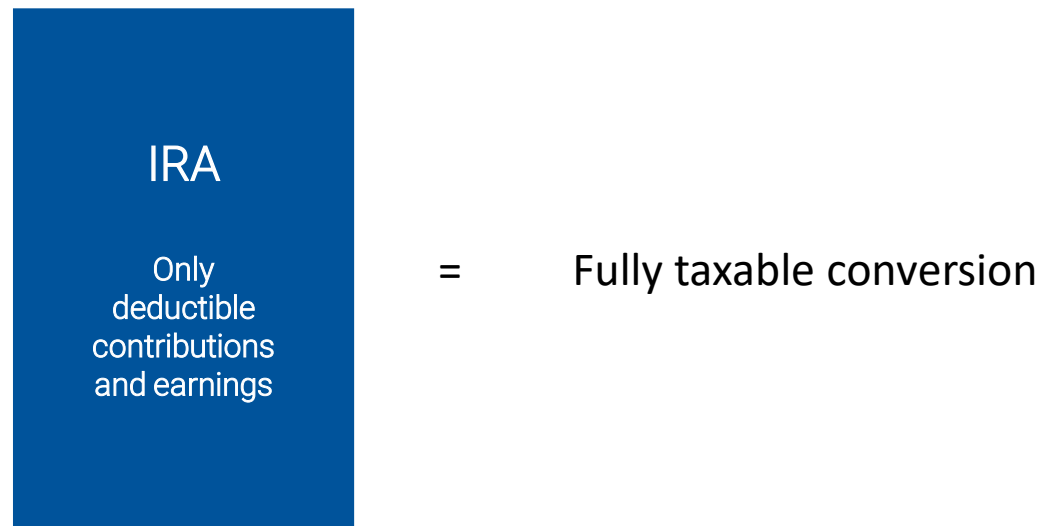
- Taxed as if you took a withdrawal from the traditional IRA
- 10% penalty tax doesn't apply (but may be recaptured if you make a nonqualified withdrawal from your Roth IRA within five years of any conversion)



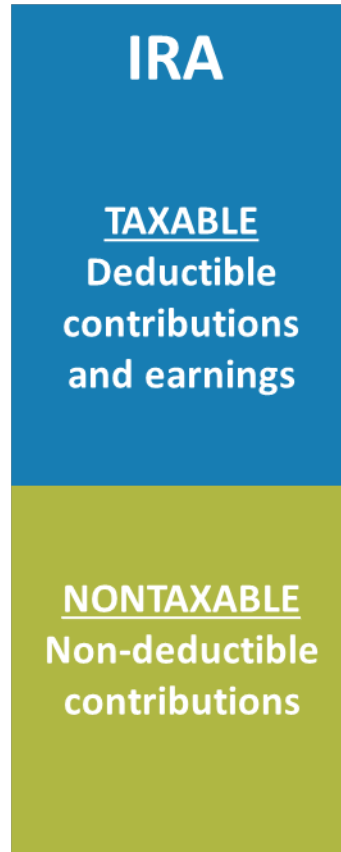
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CALCULATING THE CONVERSION TAXES

If you've made only deductible contributions to your traditional IRAs, then the entire amount you convert is subject to income tax.



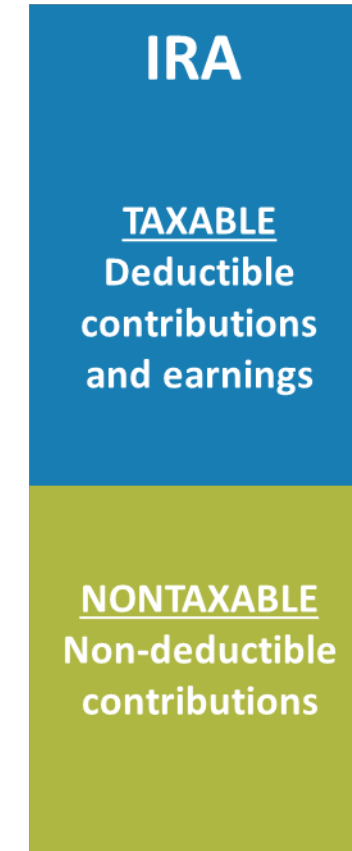
CALCULATING THE CONVERSION TAXES



- If you've made nondeductible (after-tax) contributions to your traditional IRA, any distribution consists of pro rata amount of taxable and nontaxable dollars
- Can't just convert nontaxable dollars in a traditional IRA for tax-free conversion

CALCULATING THE CONVERSION TAXES

Must aggregate all traditional IRAs you own, including SEP and SIMPLE IRAs, when calculating the taxable amount of a withdrawal or conversion



WHO CAN CONVERT TO A ROTH?

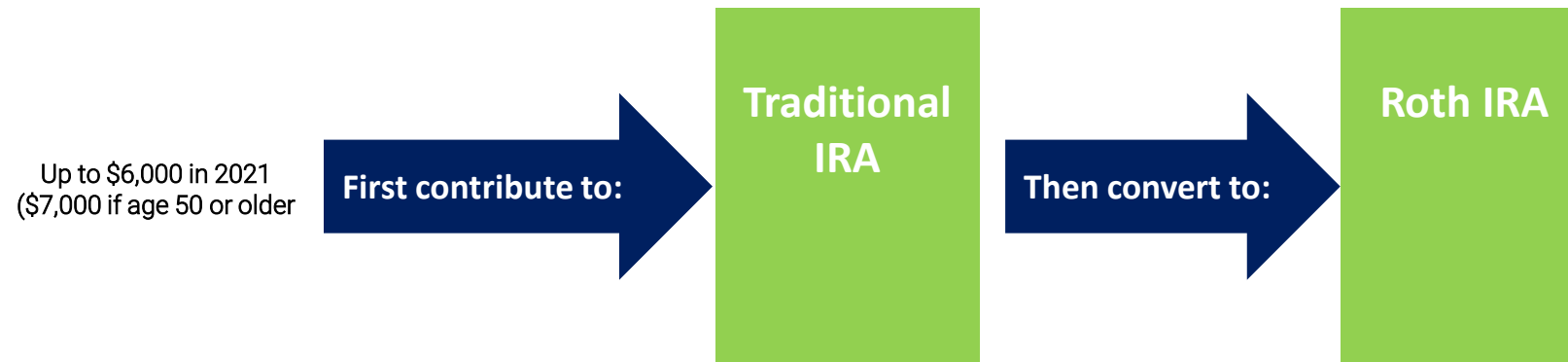
Exception

- You can't convert an inherited traditional IRA to a Roth IRA (special rules apply to spouse beneficiaries)



USING THE “BACK DOOR” TO FUND ANNUAL ROTH CONTRIBUTIONS

- Even if you can't contribute to a Roth IRA because of the income limits, you can contribute to a traditional IRA as long as you have earned income
- Anyone can convert a traditional IRA to a Roth, regardless of income or marital status
- You can make nondeductible contributions initially to a traditional IRA
- Convert that traditional IRA to a Roth
- Remember to aggregate your traditional IRAs when calculating tax



CONVERTING EMPLOYER PLAN DOLLARS TO A ROTH IRA

- Eligible distributions from 401(k), 403(b), 457(b), and qualified plans can be rolled over to traditional or Roth IRA
- Your employer will identify an eligible rollover distribution
- Amounts rolled over to a Roth IRA are taxed except for any after-tax contributions
- Anyone can roll over to a Roth IRA, regardless of income limits or marital status – even non-spouse beneficiaries
- Rollovers from employer plans can be complicated, and can have serious tax implications



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IS A ROTH IRA RIGHT FOR YOU?

Pros

- Beneficial if you expect to be in a higher tax bracket when you take payouts
- Qualified distributions are tax free, won't impact Social Security
- Lifetime distributions not required; more assets can compound tax free for longer time
- May be able to leave more to heirs, income tax free



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IS A ROTH IRA RIGHT FOR YOU?

Cons

- May not be appropriate if you expect to be in a lower tax bracket when you'll take payouts (particularly if you plan to convert funds)
 - You pay taxes now; potential negative impact on Social Security, other items
 - Using IRA funds to pay conversion taxes may have serious drawbacks
- May not be appropriate if you'll need to use the funds soon
- Risk of future law changes
- State tax treatment may differ

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THANK YOU

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