



Individual Retirement Accounts

Kinds of IRAs and Prohibited Transactions

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Kinds of IRAs

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.

Traditional IRAs

Your traditional IRA can be an individual retirement account or annuity. It can be part of either a simplified employee pension (SEP) or an employer or employee association trust account.

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 cannot accept contributions of more than the deductible amount for the year. However, rollover contributions and employer contributions to a SEP 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 cannot be used to buy a life insurance policy.
- Assets in your account cannot 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.

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.

Simplified employee pension (SEP). A SEP is a written arrangement that allows your employer to make deductible contributions to a traditional IRA (a SEP IRA) set up for you to receive such contributions. Generally, distributions from SEP IRAs are subject to the withdrawal and tax rules that apply to traditional IRAs.

Beginning 2023, SEP plans may allow employees the ability to treat employee and employer SEP contributions as Roth contributions (in whole or in part). Roth contributions are not excluded from income.

A SEP IRA is owned and controlled by the employee, and the employer makes contributions to the financial institution where the SEP IRA is maintained. The employer can decide how much to put into a SEP each year, which gives some flexibility when business conditions vary.

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. The requirements for individual retirement accounts apply to these traditional IRAs.

Deemed IRAs. A qualified employer retirement plan can maintain a separate account or annuity under the plan (a deemed IRA) to receive voluntary employee contributions. An employee's account can be treated as a traditional IRA or a Roth IRA. For this purpose, a "qualified employer plan" includes:

continued



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- A qualified pension, profit-sharing, or stock bonus plan [section 401(a) plan],
- A qualified employee annuity plan [section 403(a) plan],
- A tax-sheltered annuity plan [section 403(b) plan], and
- A deferred compensation plan (section 457 plan) maintained by a state, a political subdivision of a state, or an agency or instrumentality of a state or political subdivision of a state.

SIMPLE IRAs

A savings incentive match plan for employees (SIMPLE) plan is a tax-favored written agreement (salary reduction) between you and your employer that allows you to choose to reduce your compensation (salary) by a certain percentage each pay period, and have your employer contribute the salary reductions to a SIMPLE IRA on your behalf.

Beginning 2023, SIMPLE IRAs may also accept Roth contributions, which are not excluded from income.

All contributions under a SIMPLE IRA plan must be made to a SIMPLE IRA, not to any other type of IRA.

If your employer maintains a SIMPLE IRA plan, you must be notified, in writing, that you can choose the financial institution that will serve as trustee for your SIMPLE IRA and that you can roll over or transfer your SIMPLE IRA to another financial institution.

Roth IRAs

A Roth IRA can be either an individual retirement account or individual retirement annuity, described earlier. To be a Roth IRA, the account or annuity must be designated as a Roth IRA when it is opened.

Designated Roth accounts. Designated Roth accounts are separate accounts under 401(k), 403(b), or 457(b) plans that accept elective deferrals that are referred to as Roth contributions. These elective deferrals are included in your income, but qualified distributions from these accounts are not included in your income. Designated Roth accounts are not IRAs and should not be confused with Roth IRAs. Contributions, up to their respective limits, can be made to Roth IRAs and designated Roth accounts according to your eligibility to participate. A contribution to one does not impact your eligibility to contribute to the other.

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Prohibited Transactions

Generally, a prohibited transaction is any improper use of your IRA account or annuity by you, your beneficiary, or any disqualified person.

Disqualified persons include your fiduciary and members of your family (spouse, ancestor, lineal descendant, and any spouse of a lineal descendant). The following are some examples of prohibited transactions with an IRA.

- Borrowing money from it.
- Selling property to it.
- Using it as security for a loan.
- Buying property for personal use (present or future) with IRA funds.

Fiduciary. A fiduciary is anyone who:

- Exercises any discretionary authority or discretionary control in managing your IRA or exercises any authority or control in managing or disposing of its assets.
- Provides investment advice to your IRA for a fee, or has any authority or responsibility to do so.
- Has any discretionary authority or discretionary responsibility in administering your IRA.

Effect on an IRA account. Generally, if you or your beneficiary engages in a prohibited transaction in connection with your traditional IRA account at any time during the year, the account stops being an IRA as of the first day of that year and the account is treated as distributing all its assets to you at their fair market values on the first day of the year. If the total of those values is more than your basis in the IRA, you will have a taxable gain that is includible in your income. The distribution may be subject to additional taxes or penalties.

Prohibited investments. If your traditional IRA invests in collectibles, the amount invested is considered distributed in the year the investment is made. An early distribution penalty may also apply. Collectibles are things like artworks, antiques, gems, stamps, and coins. However certain coins and bullion are allowed.

Contact Us

There are many events that occur during the year that can affect your tax situation. Preparation of your tax return involves summarizing transactions and events that occurred during the prior year. In most situations, treatment is firmly established at the time the transaction occurs. However, negative tax effects can be avoided by proper planning. Please contact us in advance if you have questions about the tax effects of a transaction or event, including the following:

- Pension or IRA distributions.
- Significant change in income or deductions.
- Job change.
- Marriage.
- Attainment of age 59½ or 73.
- Sale or purchase of a business.
- Sale or purchase of a residence or other real estate.
- Retirement.
- Notice from IRS or other revenue department.
- Divorce or separation.
- Self-employment.
- Charitable contributions of property in excess of \$5,000.