Congressional Research Service
Informing the legislative debate since 1914

Traditional and Roth Individual Retirement Accounts (IRAs): A Primer

Updated May 11, 2018

Congressional Research Service
https://crsreports.congress.gov
RL34397

CRS REPORT
Prepared for Members and
Committees of Congress

Summary

In response to concerns over the adequacy of retirement savings, Congress has created incentives to encourage individuals to save more for retirement through a variety of retirement plans. Some retirement plans are employer-sponsored, such as 401(k) plans, and others are established by individual employees, such as Individual Retirement Accounts (IRAs).

This report describes the primary features of two common retirement savings accounts that are available to individuals. Although the accounts have many features in common, they differ in some important aspects. Both traditional and Roth IRAs offer tax incentives to encourage individuals to save for retirement. Contributions to traditional IRAs may be tax-deductible for taxpayers who (1) are not covered by a retirement plan at their place of employment or (2) have income below specified limits. Contributions to Roth IRAs are not tax-deductible and eligibility is limited to those with incomes under specified limits.

The tax treatment of distributions from traditional and Roth IRAs differs. Distributions from traditional IRAs are generally included in taxable income whereas distributions from Roth IRAs are not included in taxable income. Some distributions may be subject to an additional 10% tax penalty, unless the distribution is for a reason specified in the Internal Revenue Code (for example, distributions from IRAs after the individual is aged 59½ or older are not subject to the early withdrawal penalty).

Individuals may roll over eligible distributions from other retirement accounts (such as an account balance from a 401(k) plan upon leaving an employer) into IRAs. Rollovers preserve retirement savings by allowing investment earnings on the funds in the retirement accounts to accrue on a tax-deferred basis, in the case of traditional IRAs, or a tax-free basis, in the case of Roth IRAs. A provision in P.L. 115-97 (originally called the Tax Cuts and Jobs Act) repealed a special rule that allowed IRA contributions to one type of IRA to be recharacterized as contributions to the other type of IRA.

The Retirement Savings Contribution Credit (also known as the Saver's Credit) is a nonrefundable tax credit of up to $1,000. It was authorized in 2001 to encourage retirement savings among individuals with income under specified limits.

This report explains the eligibility requirements, contribution limits, tax deductibility of contributions, and rules for withdrawing funds from the accounts, and provides data on the account holdings. It also describes the Saver's Credit and provisions enacted after the Gulf of Mexico hurricanes in 2005, the Midwestern storms in 2008, and the hurricanes in 2012 and 2017 to exempt distributions to those affected by the disasters from the 10% early withdrawal penalty.

Contents

Introduction 1
Traditional IRAs 1
Eligibility 2
Contributions 2
Investment Options 2
Deductibility of Contributions 3
Withdrawals 4
Early Distributions 5
Rollovers 5
Rollovers Limited to One Per Year 6
Inherited IRAs 6
Roth IRAs 7
Eligibility and Contribution Limits 7
Investment Options 8
Conversions and Rollovers 9
Withdrawals 9
Return of Regular Contributions 9
Qualified Distributions 9
Nonqualified Distributions 10
Distributions After Roth IRA Owner's Death 10
Retirement Savings Contribution Credit 10
Data on IRA Assets, Sources of Funds, and Ownership 11

Tables

Table 1. Deductibility of IRA Contributions for Individuals Not Covered by a Plan at Work for 2017 and 2018 3
Table 2. Deductibility of IRA Contributions for Individuals Covered by a Plan at Work for 2017 and 2018 4
Table 3. Inherited IRA Distribution Rules 7
Table 4. Roth IRA Eligibility and Annual Contribution Limits for 2017 and 2018 8
Table 5. Retirement Saving Contribution Credit Income Limits for 2017 and 2018 11
Table 6. Traditional and Roth IRAs: End of Year Assets 12
Table 7. Distribution of Individual Retirement Account (IRA) Balances in 2016 12
Table 8. Ownership and Account Balances for IRAs in 2016 13

Appendixes

Appendix. Qualified Distributions Related to Natural Disasters 15

Contacts

Author Information 16
Acknowledgments 16

Introduction

Individual Retirement Accounts (IRAs) are tax-advantaged accounts that individuals (or married couples) can establish to accumulate funds for retirement. Depending on the type of IRA, contributions may be made on a pretax or post-tax basis, and investment earnings are either tax-deferred or tax-free.[1]

IRAs were first authorized by the Employee Retirement Income Security Act of 1974 (ERISA; P.L. 93-406). Originally limited to workers without pension coverage, all workers and spouses were made eligible for IRAs by the Economic Recovery Act of 1981 (P.L. 97-34). The Tax Reform Act of 1986 (P.L. 99-514) limited the eligibility for tax-deductible contributions to individuals whose employers do not sponsor plans and to those whose employers sponsor plans but who have earnings below certain thresholds. The Taxpayer Relief Act of 1997 (P.L. 105-34) allowed for certain penalty-free withdrawals and authorized the Roth IRA, which provides tax-free growth from after-tax contributions.

The Economic Growth and Tax Relief Reconciliation Act of 2001 (P.L. 107-16) significantly affected the contribution limits in these plans in three ways: (1) it increased the limits, (2) it indexed the limits to inflation, and (3) it allowed for individuals aged 50 and older to make additional "catch-up" contributions. Among other provisions, the Pension Protection Act of 2006 (P.L. 109-280) temporarily allowed for tax-free distributions for charitable contributions; made permanent the indexing of contribution limits to inflation; and allowed taxpayers to direct the Internal Revenue Service (IRS) to deposit tax refunds directly into an IRA.[2]

This report describes the two kinds of IRAs that individual workers can establish: traditional IRAs and Roth IRAs.[3] It describes the rules regarding eligibility, contributions, and withdrawals. It also describes a tax credit for retirement savings contributions. An **Appendix** explains rules related to penalty-free distributions for those affected by the 2005 Gulf of Mexico hurricanes and the 2008 Midwestern floods. The Appendix also describes relief provided by the IRS to those affected by Hurricane Sandy in 2012 and Hurricanes Harvey, Irma, and Maria in 2017.

Traditional IRAs

Traditional IRAs are funded by workers' contributions, which may be tax-deductible. The contributions accrue investment earnings in an account, and these earnings are used as a basis for retirement income. Among the benefits of traditional IRAs, two are (1) pretax contributions, which provide larger bases for accumulating investment earnings and, thus, provide larger account balances at retirement than if the money had been placed in taxable accounts; and (2) taxes are paid when funds are distributed. Since income tax rates in retirement are often lower than during working life, traditional IRA holders are likely to pay less in taxes when contributions are withdrawn than when the income was earned.

---

[1] For more information on the tax treatment of retirement savings, including Individual Retirement Accounts (IRAs), see U.S. Congress, Joint Committee on Taxation, *Present Law And Background Relating To The Tax Treatment Of Retirement Savings*, prepared by Joint Committee on Taxation, 112th Cong., 2nd sess., April 13, 2012, JCX-32-12.

[2] See also 26 U.S.C. §408 for traditional IRAs and 26 U.S.C. §408A for Roth IRAs.

[3] There are also two kinds of IRAs established by employers for employees in small businesses: Simplified Employee Pensions (SEP-IRA) and Savings Incentive Match Plans for Employees (SIMPLE-IRA). These are not discussed in this report.

Eligibility

Individuals under 70½ years old in a year and who receive taxable compensation can set up and contribute to IRAs. Examples of compensation include wages, salaries, tips, commissions, self-employment income, nontaxable combat pay, and alimony (which is treated as compensation for IRA purposes).[4] Individuals who receive income only from noncompensation sources cannot contribute to IRAs.

Contributions

Individuals may contribute either their gross compensation or the contribution limit, whichever is lower. In 2018, the annual contribution limit is $5,500, unchanged from 2017. Since 2009, the contribution limit has been subject to cost of living adjustments, but the change was insufficient to necessitate a change in 2018.[5] Individuals aged 50 and older may make additional annual $1,000 catch-up contributions. For households that file a joint return, spouses may contribute an amount equal to the couple's total compensation (reduced by the spouse's IRA contributions) or the contribution limit ($5,500 each, if younger than the age of 50, and $6,500 each, if 50 years or older), whichever is lower. Contributions that exceed the contribution limit and are not withdrawn by the due date for the tax return for that year are considered excess contributions and are subject to a 6% "excess contribution" tax. Contributions made between January 1 and April 15 may be designated for either the current year or the previous year.

Because IRAs were intended for workers without an employer-sponsored pension to save for retirement, contributions to an IRA may only come from work income, such as wages and tips. The following noncompensation sources of income cannot be used for IRA contributions:

- earnings from property, interest, or dividends;
- pension or annuity income;
- deferred compensation;
- income from partnerships for which an individual does not provide services that are a material income-producing factor; and
- foreign earned income.

Investment Options

IRAs can be set up through many financial institutions, such as banks, credit unions, mutual funds, life insurance companies, or stock brokerages. Individuals have an array of investment choices offered by the financial institutions and can transfer their accounts to other financial institutions at will.

Several transactions could result in additional taxes or the loss of IRA status. These transactions include borrowing from IRAs; using IRAs as collateral for loans; selling property to IRAs; and investing in collectibles like artwork, antiques, metals, gems, stamps, alcoholic beverages, and most coins.[6]

---

[4] See *Tax Topic Number 451 - Individual Retirement Arrangements (IRAs)*, https://www.irs.gov/taxtopics/tc451.

[5] 26 U.S.C. §415 requires the adjustments be made with procedures used to adjust Social Security benefit amounts. For more information on Social Security adjustments see CRS Report 94-803, *Social Security: Cost-of-Living Adjustments*.

[6] Gold, silver, and platinum coins issued by the U.S. Treasury, and gold, silver, palladium, and platinum bullion are permissible.

Deductibility of Contributions

IRA contributions may be non-tax-deductible, partially tax-deductible, or fully tax-deductible, depending on whether the individual or spouse is covered by a pension plan at work and their level of adjusted gross income (AGI). Individuals are covered by a retirement plan if (1) the individuals or their employers have made contributions to a defined contribution pension plan or (2) the individuals are eligible for a defined benefit pension plan (even if they refuse participation).

For individuals and households *not* covered by a pension plan at work, **Table 1** contains the income levels at which they may deduct all, some, or none of their IRA contributions, depending on the spouse's pension coverage and the household's AGI. Individuals without employer-sponsored pensions and, if married, whose spouse also does not have pension coverage may deduct up to the contribution limit from their income taxes regardless of their AGI.

For individuals and households who are covered by a pension plan at work, **Table 2** contains the income levels at which they may deduct all, some, or none of their IRA contributions, depending on the individual's or household's AGI.

Individuals may still contribute to IRAs up to the contribution limit even if the contribution is nondeductible. Nondeductible contributions come from post-tax income, not pretax income. One advantage to placing post-tax income in traditional IRAs is that investment earnings on nondeductible contributions are not taxed until distributed. Only contributions greater than the contribution limits as described above are considered excess contributions. Worksheets for computing partial deductions are included in "IRS Publication 590-A, Contributions to Individual Retirement Arrangements (IRAs)."[7]

Table 1. Deductibility of IRA Contributions for Individuals Not Covered by a Plan at Work for 2017 and 2018

Filing Status	2017 Adjusted Gross Income	2018 Adjusted Gross Income	Deduction Allowed
Single, head of household, qualifying widow(er), or married filing jointly or separately with a spouse who is not covered by a plan at work	Any amount	Any amount	Full deduction
Married filing jointly with a spouse who is covered by a plan at work	$186,000 or less	$189,000 or less	full deduction
	More than $186,000 but less than $196,000	More than $189,000 but less than $199,000	Partial deduction
	$196,000 or more	$199,000 or more	No deduction
Married filing separately with a spouse who is covered by a plan at work	Less than $10,000	Less than $10,000	Partial deduction
	$10,000 or more	$10,000 or more	No deduction

Source: IRS Publication 590-A, available at http://www.irs.gov/publications/p590a/ and IRS News Release IR-2017-177 available at https://www.irs.gov/newsroom/irs-announces-2018-pension-plan-limitations-401k-contribution-limit-increases-to-18500-for-2018.

[7] The publication is available on the Internal Revenue Service (IRS) website at http://www.irs.gov/publications/p590a.

Table 2. Deductibility of IRA Contributions for Individuals Covered by a Plan at Work for 2017 and 2018

Filing Status	2017 Adjusted Gross Income	2018 Adjusted Gross Income	Deduction Allowed
Single or head of household	$62,000 or less	$63,000 or less	Full deduction
	More than $62,000 but less than $72,000	More than $63,000 but less than $73,000	Partial deduction
	$72,000 or more	$73,000 or more	No deduction
Married filing jointly or qualifying widow(er)	$99,000 or less	$101,000 or less	Full deduction
	More than $99,000 but less than $119,000	More than $101,000 but less than $121,000	Partial deduction
	$119,000 or more	$121,000 or more	No deduction
Married filing separately	Less than $10,000	Less than $10,000	Partial deduction
	$10,000 or more	$10,000 or more	No deduction

Source: IRS Publication 590-A, available at http://www.irs.gov/publications/p590a/ and IRS News Release IR-2017-64 available at https://www.irs.gov/pub/irs-drop/n-17-64.pdf.

Withdrawals

Withdrawals from IRAs are subject to income tax in the year that they are received.[8] Early distributions are withdrawals made before the age of 59½. Early distributions may be subject to an additional 10% penalty.

To ensure that IRAs are used for retirement income and not for bequests, IRA holders must begin making withdrawals by April 1 of the year after reaching the age of 70½ (i.e., the required beginning date). The minimum amount that must be withdrawn (i.e., the required minimum distribution) is calculated by dividing the account balance on December 31 of the year preceding the distribution by the IRA owner's life expectancy as found in IRS Publication 590-B.[9] Although females live longer on average than males,[10] the IRS does not separate life expectancy tables for males and females for this purpose.[11] Required minimum distributions must be received by December 31 of each year. Failure to take the required minimum distribution results in a 50% excise tax on the amount not distributed as required. Congress suspended the Required Minimum Distribution (RMD) provision for 2009.[12]

[8] For a detailed explanation of withdrawals from IRAs, see CRS Report R40192, *Early Withdrawals and Required Minimum Distributions in Retirement Accounts: Issues for Congress*, by John J. Topoleski.

[9] Life expectancy is calculated differently depending on whether the account holder (1) is single and an IRA beneficiary, (2) has a spouse who is more than 10 years younger, (3) has a spouse who is not more than 10 years younger, (4) whose spouse is not the sole beneficiary, or (5) is unmarried.

[10] See, for example, the Social Security Actuarial Life Table, https://www.ssa.gov/oact/STATS/table4c6.html.

[11] The Supreme Court ruled in *Arizona Governing Comm. vs. Norris*, 463 U.S. 1073 (1983), that employer-provided pension plans must use unisex tables in calculating monthly annuity benefits. Citing this ruling, the IRS constructs its own unisex life expectancy tables. See 26 U.S.C. §417(e)(3)(A)(ii).

[12] Congress did not enact any of the proposals that were introduced to suspend the RMD in years after 2009. See CRS Report R40192, *Early Withdrawals and Required Minimum Distributions in Retirement Accounts: Issues for Congress*.

Beginning in 2007, distributions from IRAs after the age of 70½ could be made directly to qualified charities and excluded from gross income. This provision for Qualified Charitable Distributions was made permanent in P.L. 114-113.[13]

Early Distributions

Early distributions are withdrawals made before the age of 59½. Early distributions—just like distributions after the age of 59½—are subject to federal income tax. To discourage the use of IRA funds for preretirement uses, most early distributions are subject to a 10% tax penalty.[14] The early withdrawal penalty does not apply to distributions before the age of 59½ if they

- occur if the individual is a beneficiary of a deceased IRA owner;
- occur if the individual is disabled;
- are in substantially equal payments over the account holder's life expectancy;
- are received after separation from employment after the age of 55;
- are for unreimbursed medical expenses in excess of 7.5% of AGI;
- are for medical insurance premiums in the case of unemployment;
- are used for higher education expenses;
- are used to build, buy, or rebuild a first home up to a $10,000 withdrawal limit;
- occur if the individual is a reservist called to active duty after September 11, 2001;
- were distributions to residents in areas affected by Hurricanes Katrina, Rita, and Wilma from around the storms' landfalls to January 1, 2007;
- were distributions to residents in areas affected by the Midwestern floods in 2008 from after the applicable disaster date and before January 1, 2010; or
- were distributions in areas affected by Hurricanes Harvey, Irma, and Maria from around the storms' landfalls to January 1, 2019.

Although individuals may make early withdrawals from IRAs without a reason, they will be subject to the 10% tax penalty unless they meet one of the conditions above. There are no other general "hardship" exceptions for penalty-free distributions from IRAs.

Rollovers

Rollovers are transfers of assets from one retirement plan to another upon separation from the original employer. Rollovers are not subject to the 59½ rule, the 10% penalty, or the contribution limit. Rollovers can come from traditional IRAs, employers' qualified retirement plans (e.g., 401(k) plans), deferred compensation plans of state or local governments (Section 457 plans), tax-sheltered annuities (Section 403(b) plans), or the Thrift Savings Plan for federal employees.

Rollovers can be either direct trustee-to-trustee transfers[15] or issued directly to individuals who then deposit the rollovers into traditional IRAs. Individuals have 60 days from the date of the

[13] See CRS Report RS22766, *Qualified Charitable Distributions from Individual Retirement Accounts: Features and Legislative History*, by John J. Topoleski and Gary Sidor.

[14] See 26 U.S.C. §72(t).

[15] A trustee-to-trustee transfer is a transfer of funds made directly between two financial institutions. The individual does not take possession of the funds at any point.

distribution to make rollover contributions. Rollovers not completed within 60 days are considered taxable distributions and may be subject to the 10% early withdrawal penalty. In addition, in cases where individuals directly receive a rollover, 20% of the rollover is withheld for tax purposes. Direct trustee-to-trustee transfers are not subject to withholding taxes. In cases where individuals directly receive a rollover, they must have an amount equal to the 20% withheld available from other sources to place in the new IRA. If the entire distribution is rolled over within 60 days, the amount withheld is applied to individuals' income taxes paid for the year.

Rollovers Limited to One Per Year

A January 2014 U.S. Tax Court decision required that, in certain circumstances, individuals are limited to a total of one rollover per year for their IRAs.[16] Rollovers subject to this rule are those between two IRAs in which an individual receives funds from an IRA and deposits the funds into a different IRA within 60 days. The one-rollover-per-year limit applies to rollovers between two traditional IRAs or two Roth IRAs. It does not apply to rollovers from a traditional IRA to a Roth IRA. The limitation does not apply to trustee-to-trustee transfers (directly from one financial institution to another) or rollovers from qualified pension plans (such as from 401(k) plans).

Inherited IRAs

When the owner of an IRA dies, ownership passes to the account's designated beneficiary or, if no beneficiary has been named, to the decedent's estate. Federal law has different distribution requirements depending on whether the new owner is a

- designated beneficiary who is the former owner's spouse;
- designated beneficiary who is not the former owner's spouse; or
- nondesignated beneficiary.

The distribution rules are summarized in **Table 3**. The distribution rules also depend on whether the IRA owner died prior to the required beginning date, the date on which distributions from the account must begin. This is April 1 of the year following the year in which the owner of an IRA reaches the age of 70½. Distributions from inherited IRAs are taxable income but are not subject to the 10% early withdrawal penalty. Failure to take the RMD results in a 50% excise tax on the amount not distributed as required.

Designated spouse beneficiaries who treat inherited IRAs as their own can roll over inherited IRAs into traditional IRAs or, to the extent that the inherited IRAs are taxable, into qualified employer plans (such as 401(k), 403(b), or 457 plans). Nonspouse beneficiaries cannot roll over any amount into or out of inherited IRAs.

In some cases, IRAs have beneficiaries' distributions requirements that are more stringent than those summarized in **Table 3**. For example, an IRA's plan documents could require that a designated spouse or designated nonspouse beneficiary distribute all assets in the IRA by the end of the fifth year of the year following the IRA owner's death. In such a case, the beneficiary would not have the option to take distributions over a longer period of time. Unless the IRA plan documents specify otherwise, it is possible to take distributions faster than required in **Table 3**. For example, a beneficiary may elect to distribute all assets in a single year. In such a case, the entire amount distributed is taxable income for that year.

[16] See *Bobrow v.Commissioner*, T.C. Memo. 2014-21 (United States Tax Court 2014), available at http://www.ustaxcourt.gov/InOpHistoric/bobrowmemo.nega.TCM.WPD.pdf. Prior to this decision, the IRS applied the one-rollover-per-year on an IRA-by-IRA basis.

Table 3. Inherited IRA Distribution Rules

	Owner Dies Before Required Beginning Date	Owner Dies after Required Beginning Date
Spouse is named as the designated beneficiary	Treat as own, does not have to take any distribution until the age of 70½, but is subject to the 59½ rule, or Keep in decedent's name and take distributions based on own life expectancy. Distributions do not have to begin until decedent would have turned 70½.	Treat as own, does not have to take any distribution until the age of 70½, but is subject to the 59½ rule, or Keep in decedent's name and take distributions based on own life expectancy.
A nonspouse is named as the designated beneficiary	Take distributions based on life expectancy for beneficiary's age as of birthday in the year following the year of the owner's death, reduced by one for each year since owner's death. If the nonspouse beneficiary does not take a distribution in year of owner's death, then all IRA assets must be distributed by the end of the fifth year of the year following the IRA owner's death.	Take distributions based on the longer of (1) beneficiary's life expectancy, or (2) owner's life expectancy using age as of birthday in the year of death, reduced by one for year after the year of death.
Beneficiary is not named	Must distribute all IRA assets by the end of the fifth year of the year following the IRA owner's death.	Take a yearly distribution based on the owner's age as of birthday in the year of death, reduced by one for each year after the year of death.

Source: IRS Publication 590-B, available at http://www.irs.gov/publications/p590b/.

Notes: The required beginning date is the date on which distributions from the account must begin. It is April 1 of the year following the year in which the owner of an IRA reaches the age of 70½.

Roth IRAs

Roth IRAs were authorized by the Taxpayer Relief Act of 1997 (P.L. 105-34). The key differences between traditional and Roth IRAs are that contributions to Roth IRAs are made with after-tax funds and qualified distributions are not included in taxable income; investment earnings accrue free of taxes.[17]

Eligibility and Contribution Limits

In contrast to traditional IRAs, Roth IRAs have income limits for eligibility. **Table 4** lists the adjusted gross incomes at which individuals may make the maximum contribution and the ranges in which this contribution limit is reduced.[18] For example, a 40-year-old single taxpayer with income of $90,000 can contribute an annual contribution of $5,500 in 2018. A similar taxpayer making $120,000 would be subject to a reduced contribution limit, whereas a taxpayer with income of $140,000 would be ineligible to contribute to a Roth IRA.

[17] Roth IRAs are named for former Senator William Roth.

[18] If warranted, the income limits are increased for cost-of-living adjustments. See *2018 Limitations Adjusted As Provided in Section 415(d), etc.*, Notice 2017-64, https://www.irs.gov/pub/irs-drop/n-17-64.pdf.

Table 4. Roth IRA Eligibility and Annual Contribution Limits for 2017 and 2018

Filing Status	2017 Modified Adjusted Gross Income (AGI)	2017 Contribution Limits	2018 Modified Adjusted Gross Income (AGI)	2018 Contribution Limits
Single, head of household, married filing separately (and did not live with spouse at any time during the year)	Less than $118,000	$5,500 ($6,500 if 50 years or older) or AGI, whichever is smaller	Less than $120,000	$5,500 ($6,500 if 50 years or older) or AGI, whichever is smaller
	At least $118,000 but less than $133,000	Reduced contribution limit	At least $120,000 but less than $135,000	Reduced contribution limit
	$133,000 or more	Ineligible to contribute	$135,000 or more	Ineligible to contribute
Married filing separately and lived with spouse at any time during the year	Less than $10,000	Reduced contribution limit	Less than $10,000	Reduced contribution limit
	$10,000 or more	Ineligible to contribute	$10,000 or more	Ineligible to contribute
Married filing jointly, qualifying widow(er)	Less than $186,000	$5,500 each ($6,500 each if 50 and older) or AGI, whichever is smaller	Less than $189,000	$5,500 each ($6,500 each if 50 and older) or AGI, whichever is smaller
	At least $186,000 but less than $196,000	Reduced contribution limit	At least $189,000 but less than $199,000	Reduced contribution limit
	$196,000 or more	Ineligible to contribute	$199,000 or more	Ineligible to contribute

Source: IRS Publication 590-A, available at http://www.irs.gov/publications/p590a/ and IRS News Release IR-2017-64 available at https://www.irs.gov/pub/irs-drop/n-17-64.pdf.

Individuals aged 50 and older can make additional $1,000 catch-up contributions. The AGI limit for eligibility has been adjusted for inflation since 2007; beginning in 2009, the traditional and Roth IRA contribution limit has also been adjusted for inflation. A worksheet for computing reduced Roth IRA contribution limits is provided in IRS Publication 590-A.

Investment Options

Roth IRAs must be designated as such when they are set up. As with traditional IRAs, they can be set up through many financial institutions. Transactions prohibited within traditional IRAs are also prohibited within Roth IRAs.

Conversions and Rollovers

Individuals may convert amounts from traditional IRAs, SEP-IRAs, or SIMPLE-IRAs[19] to Roth IRAs.[20] Since 2008, individuals have been able to roll over distributions directly from qualified retirement plans to Roth IRAs. The amount of the conversion must be included in taxable income. Conversions can be a trustee-to-trustee transfer, a same trustee transfer by redesignating the IRA as a Roth IRA, or a rollover directly to the account holder. Inherited IRAs cannot be converted.

A provision in P.L. 115-97 (originally called the Tax Cuts and Jobs Act) repealed a special rule that allowed IRA contributions to one type of IRA to be recharacterized as a contribution to the other type of IRA. Prior to the repeal of the special rule, an individual could have made contributions to a traditional IRA and then, prior to the due date of the individual's tax return, could have transferred to the assets to a Roth IRA. In certain circumstances, this could have a beneficial effect on an individual's taxable income. Recharacterization of IRA contributions for the 2017 tax year can be completed by October 15, 2018.[21]

The rules for rollovers that apply to traditional IRAs, including completing a rollover within 60 days, also apply. Additionally, withdrawals from a converted IRA prior to five years from the beginning of the year of conversion are nonqualified distributions and are subject to a 10% penalty.

Tax-free withdrawals from one Roth IRA transferred to another Roth IRA are allowed if completed within 60 days. Rollovers from Roth IRAs to other types of IRAs or to employer-sponsored retirement plans are not allowed.

Withdrawals

The three kinds of distributions from Roth IRAs are (1) return of regular contributions, (2) qualified distributions, and (3) nonqualified distributions. Returns of regular contributions and qualified distributions are not included as part of taxable income.

Return of Regular Contributions

Distributions from Roth IRAs that are a return of regular contributions are not included in gross income nor are they subject to the 10% penalty on early distributions.

Qualified Distributions

Qualified distributions must satisfy both of the following:

- they are made after the five-year period beginning with the first taxable year for which a Roth IRA contribution was made,[22] and

[19] Simplified Employee Pensions (SEP-IRA) and Savings Incentive Match Plans for Employees (SIMPLE-IRA) are IRAs established by employers for employees in small businesses.

[20] Prior to January 1, 2010, only individuals with income under specified thresholds were eligible to make conversions from traditional to Roth IRAs. The Tax Increase Prevention and Reconciliation Act of 2005 (TIPRA; P.L. 109-222) eliminated the income thresholds.

[21] For more information, see Joint Committee on Taxation, *Description Of H.R.1, The "Tax Cuts And Jobs Act",* JCX-50-17, November 3, 2017, pp. 72 - 75, https://www.jct.gov/publications.html?func=startdown&id=5031.

[22] The five-year period is not necessarily five calendar years. Contributions made from January 1 to April 15 could be considered made in the previous tax year.

- they are made on or after the age of 59½; because of disability; to a beneficiary or estate after death; or to purchase, build, or rebuild a first home up to a $10,000 lifetime limit.

Nonqualified Distributions

Distributions that are neither returns of regular contributions nor qualified distributions are considered nonqualified distributions. Although individuals might have several Roth IRAs from which withdrawals can be made, for tax purposes nonqualified distributions are assumed to be made in the following order:

1. the return of regular contributions,
2. conversion contributions on a first-in-first-out basis, and
3. earnings on contributions.

Nonqualified distributions may have to be included as part of income for tax purposes. A worksheet is available in IRS Publication 590-B to determine the taxable portion of nonqualified distributions. A 10% penalty applies to nonqualified distributions unless one of the exceptions in 26 U.S.C. Section 72(t) applies. The exceptions are identical to those previously listed for early withdrawals from traditional IRAs.

Distributions After Roth IRA Owner's Death

If the owner of a Roth IRA dies, the distribution rules depend on whether the beneficiary is the spouse or a nonspouse. If the beneficiary is the spouse, then the spouse becomes the new owner of the inherited Roth IRA. If the spouse chooses not to treat the inherited Roth IRA as their own, or if the beneficiary is a nonspouse, then there are two options. The beneficiary can distribute the entire interest in the Roth IRA (1) by the end of the fifth calendar year after the year of the owner's death, or (2) over the beneficiary's life expectancy. As with an inherited traditional IRA, a spouse can delay distributions until the decedent would have reached the age of 70½.

Distributions from inherited Roth IRAs are generally free of income tax. The beneficiary may be subject to taxes if the owner of a Roth IRA dies before the end of (1) the five-year period beginning with the first taxable year for which a contribution was made to a Roth IRA or (2) the five-year period starting with the year of a conversion from a traditional IRA to a Roth IRA. The distributions are treated as described in the "Nonqualified Distributions" section of this report.

Retirement Savings Contribution Credit

The Economic Growth and Tax Relief Reconciliation Act of 2001 (P.L. 107-16) authorized a nonrefundable tax credit of up to $1,000 for eligible individuals, or $2,000 if filing a joint return, who contribute to IRAs or employer-sponsored retirement plans.[23] The Retirement Savings Contribution Credit, also referred to as the Saver's Credit, is in addition to the tax deduction for contributions to traditional IRAs or other employer-sponsored pension plans. To receive the credit, taxpayers must be at least 18 years old, not full-time students, not an exemption on someone else's tax return, and have AGI less than certain limits. The limits are in **Table 5**. For example, individuals who make a $2,000 IRA contribution in 2018, have income of $15,000, and list their filing status as single would be able to reduce their 2018 tax liability by up to $1,000.

[23] See also CRS Report RS21795, *The Retirement Savings Tax Credit: A Fact Sheet*, by John J. Topoleski.

Taxpayers must file form 1040, 1040A, or 1040NR. The Saver's Credit is not available on form 1040EZ, which may limit the use of the credit.

Table 5. Retirement Saving Contribution Credit Income Limits for 2017 and 2018

Filing Status	2017 Income Limits	2018 Income Limits	Percentage Credit
Single, Married Filing Separately, Qualifying Widow(er)	$1 to $18,500	$1 to $19,000	50%
	$18,501 to $20,000	$19,001 to $20,500	20%
	$20,001 to $31,000	$20,501 to $31,500	10%
	more than $31,000	more than $31,500	0%
Head of Household	$1 to $27,750	$1 to $28,500	50%
	$27,751 to $30,000	$28,501 to $30,750	20%
	$30,001 to $46,500	$30,751 to $47,250	10%
	more than $46,500	more than $47,250	0%
Married Filing Jointly	$1 to $37,000	$1 to $38,000	50%
	$37,001 to $40,000	$38,001 to $41,000	20%
	$40,001 to $62,000	$41,001 to $63,000	10%
	more than $62,000	more than $63,000	0%

Source: IRS Publication 590-A, available at http://www.irs.gov/publications/p590a/ and IRS News Release IR-2017-64 available at https://www.irs.gov/pub/irs-drop/n-17-64.pdf.

Data on IRA Assets, Sources of Funds, and Ownership

Table 6 contains data on the end-of-year assets in traditional and Roth IRAs from 2005 to 2016. According to the Investment Company Institute, traditional IRAs held much more in assets than Roth IRAs. At the end of 2016, there was $6.7 trillion held in traditional IRAs and $660 billion held in Roth IRAs. Within traditional IRAs, more funds flowed from rollovers from employer-sponsored pensions compared with funds from regular contributions.[24] For example, in 2014 (the latest year for which such data are available) funds from rollovers were $423.9 billion, whereas funds from contributions were only $17.5 billion.[25] However, within Roth IRAs in 2014 more funds flowed from contributions ($21.9 billion in 2014) than from rollovers ($5.7 billion in 2014).[26]

[24] Generally, rollovers are tax-free distributions of assets from one retirement plan that are contributed to a second retirement plan. Regular contributions are contributions to IRAs that are made from individuals' pre- or post-tax income (subject to the rules of the particular type of IRA).

[25] See the Investment Company Institute, The U.S. Retirement Market, Third Quarter 2017, Table 9, available at https://www.ici.org/info/ret_17_q3_data.xls.

[26] See the Investment Company Institute, The U.S. Retirement Market, Third Quarter 2017, Table 10, available at https://www.ici.org/info/ret_17_q3_data.xls.

Table 6. Traditional and Roth IRAs: End of Year Assets

(in billions of dollars)

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Traditional IRAs	3,034	3,722	4,187	3,257	3,941	4,340	4,531	5,109	6,019	6,421	6,254	6,695
Roth IRAs	156	196	232	177	239	355	365	420	505	550	605	660

Source: The Congressional Research Service (CRS) table using data from the Investment Company Institute, The U.S. Retirement Market, Third Quarter 2017, Table 8, available at https://www.ici.org/info/ret_17_q3_data.xls.

Table 7 and **Table 8** provide additional data on IRA ownership amounts among U.S. households. The data are from CRS analysis of the 2016 Survey of Consumer Finances (SCF).[27] The SCF is a triennial survey conducted on behalf of the Board of Governors of the Federal Reserve and contains detailed information on U.S. household finances, such as the amount and types of assets owned, the amount and types of debt owed, and detailed demographic information on the head of the household and spouse. The SCF is designed to be nationally representative of the 126.0 million U.S. households in 2016.

Table 7 categorizes IRAs by the amount in the account. Among households that have IRAs, 61.1% have account balances of less than $100,000 and 4.4% have account balances of $1 million or more.[28]

Table 7. Distribution of Individual Retirement Account (IRA) Balances in 2016

	Percentage of All U.S. Households	Percentage of U.S. Households with IRAs
No IRA	70.2%	-
Account balance		
$1 to $24,999	10.6%	35.6%
$25,000 to $49,999	3.7%	12.4%
$50,000 to $99,999	3.9%	13.1%
$100,000 to $249,999	5.5%	18.3%
$250,000 to $999,999	4.8%	16.1%
$1,000,000 to $2,499,999	1.1%	3.8%
$2,500,000 or more	0.2%	0.6%

Source: CRS analysis of 2016 Survey of Consumer Finances.

Notes: Analysis does not include households with Keogh accounts.

Table 8 provides data on IRA ownership and account balances among households that owned IRAs in 2016.

The following are some key points from **Table 8** regarding ownership of IRAs:

- In 2016, 29.8% of U.S. households had an IRA. Among households that owned IRAs, the median account balance ($52,000) was smaller than the average

[27] More information on the SCF is available at http://www.federalreserve.gov/econresdata/scf/scfindex.htm.

[28] 35.6% + 12.4% + 13.1% = 61.1%

account balance ($201,240), which indicates that some households likely had very large IRA account balances.

- Households were more likely to own IRAs as the age of head of household increased. The median and average account balances also increased as the head of the household increased.
- The percentage of households with an IRA and the median and average account balances increased with the income of the household. Among the explanations for this finding are that (1) households with more income are better able to save for retirement and (2) households with higher income are more likely to participate in a defined contribution (DC) plan (like a 401(k)) and therefore have an account to roll over.[29]
- Married households were more likely to have an IRA than single households and their median and average account balances were also larger. The explanations could include the following: both spouses in a married household might have work histories, enabling both to save for retirement or married household might need larger retirement savings because two people would be using the retirement savings for living expenses in retirement.

Table 8. Ownership and Account Balances for IRAs in 2016

	Percentage of U.S. Households with Account	Median Account Balance	Average Account Balance
All Households	29.8%	$52,000	$201,240
Age of the Head of the Household:			
Younger than 35	15.8%	$10,000	$22,296
35 to 44	26.7%	$30,000	$72,706
45 to 54	30.5%	$48,000	$132,287
55 to 64	37.9%	$88,000	$277,970
65 and older	38.1%	$117,000	$317,474
Household Income:			
Less than $30,000	8.7%	$16,000	$54,430
$30,000 to $49,999	19.3%	$31,700	$71,670
$50,000 to $74,999	28.7%	$32,000	$116,001
$75,000 to $124,999	41.7%	$39,500	$136,682
$125,000 or more	64.9%	$140,000	$361,951
Household Marital Status:			
Married	36.3%	$68,000	$236,711
Single	21.3%	$32,000	$122,150

Source: CRS analysis of the 2016 Survey of Consumer Finances.

Note: Median and average account balances are calculated among households that owned IRAs.

[29] See CRS Report R43439, *Worker Participation in Employer-Sponsored Pensions: A Fact Sheet*.

Appendix. Qualified Distributions Related to Natural Disasters

As part of the response to the 2005 hurricanes that affected the communities on and near the Gulf of Mexico, Congress approved provisions that exempted individuals affected by the storms from the 10% early withdrawal penalty for withdrawals from IRA. In 2008, Congress approved similar provisions in response to the storms and flooding in certain Midwestern states. Following Hurricane Sandy in October 2012, the California wildfires in 2017, and the hurricanes in 2017, the Internal Revenue Service (IRS) eased certain requirements for hardship distributions from defined contribution plans. However, the IRS was unable to exempt distributions from retirement plans from the 10% early withdrawal penalty because such an exemption requires congressional authorization.

Qualified Distributions Related to Hurricanes Katrina, Rita, and Wilma

In response to Hurricanes Katrina, Rita, and Wilma, Congress approved the Gulf Opportunity Zone Act of 2005 (P.L. 109-135). The act amended the Internal Revenue Code to allow residents in areas affected by these storms who suffered economic losses to take penalty-free distributions up to $100,000 from their retirement plans, including traditional and Roth IRAs. The distributions must have been received after August 24, 2005 (Katrina), September 22, 2005 (Rita), or October 22, 2005 (Wilma), and before January 1, 2007. The distributions were taxable income and could be reported as income either in the year received or over three years (e.g., a $30,000 distribution made in May 2006, could have been reported as $10,000 of income in 2006, 2007, and 2008). Alternatively, part or all of the distribution could have been repaid to the retirement plan within three years of receiving the distribution without being considered taxable income.

Qualified Distributions Related to the Midwestern Disaster Relief Area

In response to severe storms, tornados, and flooding that occurred in certain Midwestern states, the Heartland Disaster Tax Relief Act of 2008 allowed residents of specified Midwest areas to take penalty-free distributions up to $100,000 from their retirement plans, including traditional and Roth IRAs. This act was passed as Division C of P.L. 110-343, the Emergency Economic Stabilization Act of 2008. The bill amended 26 U.S.C. 1400Q, which was enacted as part of the Gulf Opportunity Zone Act of 2005 (P.L. 109-135). The distributions must have been received after the date on which the President declared an area to be a major disaster area and before January 1, 2010.[30] Apart from the dates and the areas affected, the provisions were identical to the provisions for individuals who were affected by Hurricanes Katrina, Rita, and Wilma.

[30] The disaster areas are limited to Arkansas, Illinois, Indiana, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, and Wisconsin.

Qualified Distributions Related to Hurricanes Harvey, Irma, and Maria

In response to Hurricanes Harvey, Irma, and Maria, Congress approved the Disaster Tax Relief and Airport and Airway Extension Act of 2017 (P.L. 115-63). The act amended the Internal Revenue Code to allow residents in areas affected by these storms who suffered economic losses to take penalty-free distributions up to $100,000 from their retirement plans, including traditional and Roth IRAs. The distributions must have been made on or after August 23, 2017 (Harvey), September 4, 2017 (Irma), or September 16, 2017 (Maria), and before January 1, 2019. The distributions are taxable income and can be reported either in the year received or over three years. Alternatively, part or all of the distribution may be repaid to the retirement plan within three years of receiving the distribution without being considered taxable income.

Hurricane Sandy and California Wildfire Relief

In the cases of Hurricane Sandy in 2012 and the California wildfires in 2017 no legislation was passed that would have (1) exempted individuals in areas affected by these natural disasters from the 10% penalty for early withdrawals from IRAs or defined contribution retirement plans or (2) eased requirements for loans from defined contribution pensions for individuals affected by them.[31]

The IRS eased requirements for hardship distributions in areas affected by Hurricane Sandy in 2012 and the California wildfires in 2017. Among the relief offered by the IRS in Announcement 2012-44 and 2017-15 respectively, "Plan administrators may rely upon representations from the employee or former employee as to the need for and amount of a hardship distribution" rather than require documentation from the employee of the need.[32] The relief offered by the IRS did not include an exemption from the 10% penalty for distributions before the age of 59½. Exemptions from the 10% penalty require congressional authorization. In addition, in the announcement, the IRS suspended the provision that requires an individual to suspend contributions to 401(K) and 403(b) plans for the six months following a hardship distribution.

Author Information

John J. Topoleski
Specialist in Income Security

Acknowledgments

Emma Sifre provided research assistance.

[31] H.R. 2137, the Hurricane Sandy Tax Relief Act of 2013, introduced by Representative Bill Pascrell on May 23, 2013, and H.R. 4397, the California Wildfire Disaster Tax Relief Act of 2017, introduced by Representative Mimi Walters on November 15, 2017, would both have provided an exemption to the 10% early withdrawal penalty for retirement account distributions for those affected by Hurricane Sandy in 2012, and the California wildfires in 2017.

[32] See 26 CFR 1.401(k)-1.

Disclaimer

This document was prepared by the Congressional Research Service (CRS). CRS serves as nonpartisan shared staff to congressional committees and Members of Congress. It operates solely at the behest of and under the direction of Congress. Information in a CRS Report should not be relied upon for purposes other than public understanding of information that has been provided by CRS to Members of Congress in connection with CRS's institutional role. CRS Reports, as a work of the United States Government, are not subject to copyright protection in the United States. Any CRS Report may be reproduced and distributed in its entirety without permission from CRS. However, as a CRS Report may include copyrighted images or material from a third party, you may need to obtain the permission of the copyright holder if you wish to copy or otherwise use copyrighted material.