

# 13 Retirement, Social Security, and Medicare

## ■ Tab 13 Contents ■

IRA Limits—2024	13-1
Social Security and Medicare Highlights	13-1
Taxable Social Security Benefits Base Amounts	13-1
Pension Plan Limitations	13-2
Rollover Chart	13-2
Exceptions to the 10% Penalty on Early Distributions	13-3
Pension Plan Characteristics—2024	13-4
Pension Plan Advantages/Disadvantages—2024	13-6
Individual Retirement Arrangement (IRA)	13-7
Excess IRA Contributions	13-8
Reduced IRA Deduction	13-9
Nondeductible Contributions to IRAs	13-11
Roth IRA	13-11
Conversion Rules	13-12
Recharacterization	13-13
Simplified Employee Pension (SEP)	13-13
Savings Incentive Match Plans for Employees (SIMPLE)	13-14
Other Retirement Plans	13-16
Section 401(k) Plans	13-16
Section 403(b) Tax-Sheltered Annuity Plans	13-17
Employee Stock Ownership Plan (ESOP)	13-17
Section 457 Deferred Compensation Plans	13-17
Vesting Rules	13-17
Railroad Retirement	13-17
Rollovers and Transfers	13-19
Required Minimum Distribution (RMD)	13-21
Uniform Lifetime Table	13-21
Inherited IRA	13-22
Miscellaneous Distributions	13-23
Qualified Disaster Recovery Distributions	13-23
Pension Plans of Public Safety Employees	13-24
Qualified HSA Funding Distribution (QHFD)	13-24
Qualified Reservist Distribution	13-24
Domestic Abuse Distribution	13-24
Emergency Personal Expense Distribution	13-25
Foreign Pension and Annuity Distributions	13-25
Social Security	13-26
Taxable Social Security Benefits	13-27
How Benefits Are Calculated	13-28
How Work Affects Retirement Benefits	13-28
Medicare	13-29
Medicaid	13-30

## ■ New for 2024 ■

- **SIMPLE IRA deferral limit.** The elective deferral limit for SIMPLE IRAs is increased by 110% for certain employees. See *Increased employee elective deferral limit*, page 13-15.
- **Domestic abuse distribution.** A distribution from a retirement plan to a domestic abuse victim may not be subject to the 10% additional tax on early distributions. See *Domestic Abuse Distribution*, page 13-24.
- **Emergency personal expense distribution.** Distributions from a retirement plan for emergency expenses may not be subject to the 10% additional tax on early distributions. See *Emergency Personal Expense Distribution*, page 13-25.

## Social Security and Medicare Highlights

	2024
Social Security benefits increase	3.2%
Maximum earnings subject to:	
Social Security tax	\$168,600.00
Medicare tax	No Limit
Maximum Social Security tax:	
Employee	\$ 10,453.20
Self-employed	\$ 20,906.40
Maximum Medicare tax	No Limit
Social Security tax rate:	
Employee	6.20%
Self-employed	12.40%
Medicare tax rate:	
Employee <sup>1</sup>	1.45%
Self-employed <sup>1</sup>	2.90%
Earnings needed for one quarter of coverage	\$ 1,730.00
Additional Medicare tax on:	
Earned income above threshold <sup>1</sup>	0.9%
Unearned income above threshold <sup>1</sup>	3.8%
Maximum earnings and still receive full Social Security benefits:	
Under full retirement age <sup>2</sup>	\$ 22,320.00
Year of full retirement age <sup>3</sup>	\$ 59,520.00
Full retirement age <sup>4</sup>	No Limit
Maximum Social Security benefits at full retirement age:	
Maximum monthly benefit	\$ 3,822.00
Full retirement age <sup>4</sup>	66 & 8 mos.
Medicare premiums:	
Part A (per month)	\$ 505.00
Part B (per month) <sup>5</sup>	\$ 174.70
Hospital deductible	\$ 1,632.00

<sup>1</sup> See *Additional Medicare Tax*, Tab 3, and *Net Investment Income Tax*, page 6-4.

<sup>2</sup> \$1 in benefits is withheld for every \$2 in earnings above limit.

<sup>3</sup> Applies only to earnings for months prior to attaining full retirement age.

<sup>4</sup> \$1 in benefits is withheld for every \$3 in earnings above the limit.

<sup>4</sup> See *Full Retirement Age* chart, page 13-28.

<sup>5</sup> Standard monthly premium. High income taxpayers see *2024 Medicare Part B Monthly Premium* chart, page 13-30.

## IRA Limits—2024 (page 13-7 and page 13-11)

<b>Individual Contribution Combined Limit—Traditional and Roth IRAs</b>			
Under age 50	\$7,000	Age 50 or older	\$8,000

### Traditional IRA Phaseouts

Taxpayer is covered by an employer retirement plan:

MFJ, QSS	Single, HOH	MFS
\$123,000 to \$143,000	\$77,000 to \$87,000	\$0 to \$10,000

Contributing spouse is not covered by an employer retirement plan but other spouse is:

MFJ	MFS
\$230,000 to \$240,000	\$0 to \$10,000

### Roth IRA Phaseouts

MFJ or QSS	\$230,000–\$240,000
Single, HOH, or MFS (lived apart from spouse all year)	\$146,000–\$161,000
MFS (lived with spouse at any time during the year)	\$0–\$10,000

## Taxable Social Security Benefits Base Amounts

MFJ	\$32,000
Single, HOH, QSS, MFS (lived apart from spouse all year)	\$25,000
MFS (lived with spouse at any time during the year)	\$0

# Pension Plan Limitations

Taxpayers may have more than one qualified plan, but the contributions to all the plans must not total more than the overall limits. Contributions are limited to the lesser of the following amounts, or 100% of a participant's compensation for the year.

		2024 (Notice 2023-75)	2023 (Notice 2022-55)
<b>Traditional IRA and Roth IRA</b> <sup>1</sup>	Under age 50.....	\$7,000	\$6,500
	Age 50 or older.....	\$8,000	\$7,500
<b>SEP IRA</b> <sup>2</sup> <i>Employees</i>	25% of wages up to .....	\$69,000	\$66,000
<b>SEP IRA</b> <i>Self-Employed</i>	20% of net self-employment (SE) income after the deduction for one-half of SE tax, up to .....	\$69,000	\$66,000
<b>SIMPLE IRA</b> <sup>3</sup> ( <i>Employees and Self-Employed</i> ) IRC §408(p), IRC §414(v)	Under age 50 = Elective deferrals up to .....	\$16,000 <sup>4</sup>	\$15,500
	Age 50 or older = Elective deferrals up to .....	\$19,500 <sup>4</sup>	\$19,000
	Employer must match dollar-for-dollar up to 3% <sup>5</sup> of the participant's earned income (no limit), or elect to match 2% of wages for all employees (including nonparticipants). If the 2% match is elected, the matching contribution cannot exceed the per employee amounts of.....	\$6,900	\$6,600
<b>401(k) Plan and SARSEP</b> <sup>2,7</sup> IRC §401(k), IRC §402(g), IRC §404(a)(3), IRC §414(v), IRC §415(c)	Under age 50 = Elective deferrals up to .....	\$23,000	\$22,500
	Age 50 or older = Elective deferrals up to .....	\$30,500	\$30,000
	Employer's deduction is limited to 25% of combined wages for all participants before reducing wages for elective deferrals (20% of net SE income, <sup>6</sup> after one-half SE tax deduction in the case of a self-employed individual). The total of employer and employee contributions cannot exceed the lesser of 100% of employee's compensation or .....	\$69,000 <i>See Note, below</i>	\$66,000 <i>See Note, below</i>
<b>403(b) Plan</b> <sup>2</sup> IRC §402(g), IRC §403(b), IRC §414(v), IRC §415(c)	Under age 50 = Elective deferrals up to .....	\$23,000	\$22,500
	Age 50 or older = Elective deferrals up to .....	\$30,500	\$30,000
	Employees with at least 15 years of service with certain exempt organizations may qualify for up to \$3,000 of additional contributions under IRC section 402(g)(7). The total of employer and employee contributions cannot exceed the lesser of 100% of employee's compensation or .....	\$69,000 <i>See Note, below</i>	\$66,000 <i>See Note, below</i>
<b>Defined Contribution Plan</b> <sup>2</sup> IRC §401(a)(17), IRC §404(a)(3), IRC §415(c)	Employer's deduction is limited to 25% of combined wages for all participants (20% of net SE income <sup>6</sup> after one-half SE tax deduction in the case of a self-employed individual). The total of employer and employee contributions cannot exceed the lesser of 100% of employee's compensation or .....	\$69,000 <i>See Note, below</i>	\$66,000 <i>See Note, below</i>
	Compensation limit.....	\$345,000	\$330,000
<b>Defined Benefit Plan</b> <sup>2</sup> IRC §401(a), IRC §415(b)	Maximum deductible amount is not less than the excess (if any) of 150% of the plan's current liability, over the value of plan assets. (There are exceptions.)		
	Maximum annual distributions from the plan cannot exceed 100% of the participant's average compensation for the highest three years, or.....	\$275,000	\$265,000
	Compensation limit.....	\$345,000	\$330,000

<sup>1</sup> Compensation for purposes of a traditional IRA or Roth IRA includes wages and salaries, commissions, self-employment income, taxable alimony and separate maintenance, and nontaxable combat pay.

<sup>2</sup> Compensation for other employer-provided plans is defined in the plan document.

<sup>3</sup> Compensation for purposes of a SIMPLE IRA includes wages, tips, and other pay from the employer that is subject to income tax withholding.

<sup>4</sup> **New for 2024:** Increased amounts may apply in limited situations. See *Increased employee elective deferral limit*, page 13-15.

<sup>5</sup> Employer can elect a lower percentage, but not lower than 1%, for any two out of five years.

<sup>6</sup> Earned income for a self-employed individual means net earnings from self employment minus the deduction for the pension plan contribution [IRC §401(c)(2)(A)(v)]. **Example:** 20% of \$10,000 = 25% of \$8,000.

<sup>7</sup> SARSEPs cannot be established after 1996. Existing SARSEPs can continue to have contributions made each year.

**Note:** If permitted by the plan, participants age 50 or older can make catch-up contributions which raise the overall contribution limit. For 2024, the overall limit is \$76,500 (including \$7,500 catch-up contributions) for 401(k) [other than SIMPLE 401(k)], 403(b), and SARSEP plans.

## Rollover Chart

<i>From</i> \ <i>To</i>	Roth IRA <sup>2</sup>	Traditional IRA	SIMPLE IRA	SEP IRA	Governmental 457(b) Plan <sup>8</sup>	Qualified Plan <sup>3</sup> (pre-tax)	403(b) Plan (pre-tax)	Designated Roth Account	409A Plan <sup>4</sup>
<b>Roth IRA</b>	Yes <sup>1</sup>	No	No	No	No	No	No	No	No
<b>Traditional IRA</b>	Yes <sup>5</sup>	Yes <sup>1</sup>	Yes <sup>1,10</sup>	Yes <sup>1</sup>	Yes <sup>6</sup>	Yes	Yes	No	No
<b>SIMPLE IRA</b>	Yes <sup>5,10</sup>	Yes <sup>1,10</sup>	Yes <sup>1</sup>	Yes <sup>1,10</sup>	Yes <sup>6,10</sup>	Yes <sup>10</sup>	Yes <sup>10</sup>	No	No
<b>SEP IRA</b>	Yes <sup>5</sup>	Yes <sup>1</sup>	Yes <sup>1,10</sup>	Yes <sup>1</sup>	Yes <sup>6</sup>	Yes	Yes	No	No
<b>Governmental 457(b) Plan</b> <sup>8</sup>	Yes <sup>5</sup>	Yes	Yes <sup>10</sup>	Yes	Yes	Yes	Yes	Yes <sup>5,7,8</sup>	No
<b>Qualified Plan</b> (pre-tax) <sup>8</sup>	Yes <sup>5</sup>	Yes	Yes <sup>10</sup>	Yes	Yes <sup>6</sup>	Yes	Yes	Yes <sup>5,7,8</sup>	No
<b>403(b) Plan</b> (pre-tax) <sup>8</sup>	Yes <sup>5</sup>	Yes	Yes <sup>10</sup>	Yes	Yes <sup>6</sup>	Yes	Yes	Yes <sup>5,7,8</sup>	No
<b>Designated Roth Account</b>	Yes	No	No	No	No	No	No	Yes, if a direct trustee-to-trustee transfer	No
<b>409A Plan</b> <sup>4</sup>	No	No	No	No	No	No	No	No	No <sup>9</sup>

<sup>1</sup> Only one rollover in any 12-month period.

<sup>2</sup> Any after-tax contributions rolled into a Roth IRA are not taxable upon conversion.

<sup>3</sup> Defined contribution plans [i.e., 401(k), profit sharing, money purchase] and defined benefit plans.

<sup>4</sup> Nonqualified deferred compensation plan other than a 457(b) plan.

<sup>5</sup> Must include in income.

<sup>6</sup> Must have separate accounts.

<sup>7</sup> Must be an in-plan rollover.

<sup>8</sup> Any amount in a non-Roth qualified plan account can be rolled over to a Roth account in the same plan without penalty, whether or not the amount is currently distributable.

<sup>9</sup> Not as a tax-free rollover of vested contributions and earnings. Any transfer of funds from one account to another would be a taxable event.

<sup>10</sup> If 2-year participation in the SIMPLE IRA is met.

**Note:** Exceptions to rollover rules apply. See *Rollovers and Transfers*, page 13-19.

# Exceptions to the 10% Penalty on Early Distributions

**Form 5329, Additional Taxes on Qualified Plans (Including IRAs) and Other Tax-Favored Accounts.** Penalty applies to distributions taken before age 59½ unless one of the following exceptions apply. Enter the applicable exception code on line 2, Form 5329. If more than one exception applies, use code 99.

**Note:** For purposes of the exceptions to the 10% early withdrawal penalties, distributions from IRAs include the taxable portion of a Roth IRA distribution.

Type	Code	Exception to 10% Penalty	Qualified Plans 401(k), etc.	IRA, SEP IRA, SIMPLE IRA
<i>Separation from Service</i>	01	Distribution received after separation from service in or after the year reaching age 55, (age 50 or 25 years of service, whichever is earlier, for qualified public safety employees and private sector firefighters) [IRC §72(t)(2)(A)(v) and IRC §72(t)(10)(A)]. See <i>Pension Plans of Public Safety Employees</i> , page 13-24.	Yes	No
<i>Substantially Equal Periodic Payments</i>	02	Distribution as part of a series of substantially equal periodic payments (made at least annually) based on the participant's life expectancy, or the joint life expectancy of the participant and designated beneficiary. If from an employer plan, the payments must begin after separation from service. [IRC §72(t)(2)(A)(iv)]  Does not apply if payment schedule is subsequently modified before participant attains age 59½, or after participant attains age 59½ and less than five years have elapsed since first payment was received. [IRC §72(t)(4)]	Yes	Yes
<i>Disability</i>	03	Distribution due to the participant's total and permanent disability. [IRC §72(t)(2)(A)(iii)]	Yes	Yes
<i>Death</i>	04	Distribution to a beneficiary (or the estate) on or after the death of the participant. Does not apply to modified endowment contracts. [IRC §72(t)(2)(A)(ii)]	Yes	Yes
<i>Medical Expenses</i>	05	Distribution to pay for unreimbursed medical expenses to the extent allowable as an itemized deduction (over 7.5% of AGI), regardless if the participant itemizes deductions. [IRC §72(t)(2)(B)]	Yes	Yes
<i>Divorce</i>	06	Distribution to an alternate payee under a qualified domestic relations order (QDRO). [IRC §72(t)(2)(C)]	Yes	No
<i>Unemployed Health Insurance</i>	07	IRA distribution to an unemployed individual to pay for health insurance after leaving a job if the individual has received unemployment compensation for 12 consecutive weeks. A self-employed individual may qualify. [IRC §72(t)(2)(D)]	No	Yes
<i>Higher Education</i>	08	IRA distribution to pay for higher education expenses of the taxpayer, spouse, child, or grandchild. Qualifying expenses include tuition, fees, books, supplies, equipment, and room and board if at least a half-time student. [IRC §72(t)(2)(E)]	No	Yes
<i>First-Time Home Purchase</i>	09	IRA distribution up to \$10,000 (lifetime limit) to buy, build, or rebuild a first home. A first-time homebuyer has no present interest in a main home during the prior two years. If married, both taxpayer and spouse must qualify as first-time homebuyers and each may withdraw up to \$10,000. [IRC §72(t)(2)(F)]	No	Yes
<i>IRS Levy</i>	10	Distribution due to an IRS levy on the qualified retirement plan or IRA. [IRC §72(t)(2)(A)(vii)]	Yes	Yes
<i>Qualified Reservist</i>	11	Qualified reservist distribution from an IRA, or attributable to elective deferrals, made to a person called to active duty for a period of at least 180 days or for an indefinite period. [IRC §72(t)(2)(G)]	Yes	Yes
<i>Age</i>	12	Distribution on or after the date the participant turned age 59½ if box 7, Form 1099-R, incorrectly indicates it is an early distribution with codes 1, J, or S. [IRC §72(t)(2)(A)(i)]	Yes	Yes
<i>Nonqualified 457(b) Plans</i>	13	Distribution from an IRC section 457 plan which was not from a rollover from a qualified retirement plan. [IRC §72(t)(9)]	Yes	No
<i>Distribution Under Election</i>	14	Distribution from an employer plan under a written election that provides a specific schedule for distribution of the entire interest if, as of March 1, 1986, the participant separated from service and had begun receiving payments under the election.	Yes	No
<i>ESOP</i>	15	Distribution from ESOP for dividends on employer securities held by plan. [IRC §72(t)(2)(A)(vi)]	Yes	n/a
<i>Nonqualified Annuity</i>	16	Distribution from certain nonqualified annuity contracts [IRC §72(q)(2)]. For details, see IRS Pub. 575.	No	No
<i>Federal Phased</i>	17	Distributions from a phased retirement annuity or composite annuity received by an employee participating in the Federal Phased Retirement Program. [IRC §72(t)(2)(A)(viii)]	Yes for CSRS/FERS	No
<i>Auto Enrollment</i>	18	Permissible withdrawals from a plan with auto enrollment features. [IRC §414(w)(1)(B)]	Yes	Yes for SIMPLE IRA
<i>Birth or Adoption</i>	19	Distribution due to birth or adoption (other than child of taxpayer's spouse), up to \$5,000, per parent, for each birth or adoption, made within one year of the date of birth or final adoption. Distribution can be repaid within three years. [IRC §72(t)(2)(H)]. See Notice 2020-68.	Yes	Yes
<i>Terminal Illness</i>	20	Distribution due to terminal illness, made after the date a physician has certified the taxpayer has an illness or physical condition that can reasonably be expected to result in death in 84 months or less. Distribution can be repaid within three years. [IRC §72(t)(2)(L)]	Yes	Yes
<i>Corrective Distributions</i>	21	Certain corrective IRA distributions of excess contributions (and earnings) made on or before the return due date (including extensions). [IRC §72(t)(2)(A)(ix)]	n/a	Yes
<i>Domestic Abuse</i>	22	<b>New for 2024:</b> Distributions to a victim of domestic abuse during the 1-year period beginning on any date on which the individual is a victim of domestic abuse by a spouse or a domestic partner [IRC §72(t)(2)(K)]. See Notice 2024-55.	Yes	Yes
<i>Emergency Expenses</i>	23	<b>New for 2024:</b> Distributions for the purposes of meeting the unforeseeable or immediate financial needs relating to necessary personal or family emergency expenses [IRC §72(t)(2)(I)]. See Notice 2024-55.	Yes	Yes

**Disaster-Related Relief.** An exception to the 10% early withdrawal penalty applies for qualified disaster recovery distributions and qualified disaster distributions. See *Disaster-Related Relief*, page 13-21, and *Qualified Disaster Recovery Distributions*, page 13-23.

## Pension Plan Characteristics — 2024

	Qualifications	Contributions <sup>1</sup>	Deductions <sup>1</sup>	Distributions <sup>2</sup>	Due Dates	Penalties
<b>Traditional IRA</b> See page 13-7	<ul style="list-style-type: none"> <li>Any employee or self-employed individual with compensation. See <i>Compensation for IRA Contribution Purposes</i>, page 13-7.</li> <li>A participant can use the compensation of a spouse to qualify. See <i>Spousal IRA</i>, page 13-7.</li> </ul>	<ul style="list-style-type: none"> <li>Individual may decide how much, if any, to contribute on a year-by-year basis.</li> <li>Total contributions are combined with Roth IRAs to determine annual limits.</li> </ul>	Contributions are deductible if not covered by an employer retirement plan. If covered by an employer plan, the deduction is phased out when modified AGI is between certain amounts. For modified AGI phaseout ranges, see <i>Reduced IRA Deduction</i> , page 13-9.	Fully taxable if the taxpayer has no basis in the IRA. If there is basis, a portion of each distribution is a tax-free return of basis. A taxpayer cannot fully recover basis until funds from all traditional IRAs have been distributed.	<ul style="list-style-type: none"> <li>New accounts can be set up any time by return due date, no extensions.</li> <li>Contributions must be made by the return due date, no extensions.</li> </ul>	<ul style="list-style-type: none"> <li>10% penalty for early withdrawal unless exception applies.<sup>3</sup></li> <li>A 6% penalty applies to any excess contributions if excess plus earnings are not withdrawn by due date (including extensions) of return. (IRC §4973)</li> <li>25% penalty for excess accumulation if required minimum distribution (RMD) rules are not followed. (IRC §4974)<sup>4</sup></li> </ul>
<b>Roth IRA</b> See page 13-11	<ul style="list-style-type: none"> <li>Any employee or self-employed individual with compensation. See <i>Compensation for IRA Contribution Purposes</i>, page 13-7.</li> <li>A participant can use the compensation of a spouse to qualify (spousal IRA). See <i>Spousal IRA</i>, page 13-7.</li> </ul>	<ul style="list-style-type: none"> <li>Total contributions are combined with traditional IRAs to determine annual limits.</li> <li>The allowable contribution amount phases out when modified AGI is between certain amounts. See <i>Roth IRA Limits – 2024</i>, page 13-11.</li> </ul>	Roth IRA contributions are never deductible. Contributions add to the participant's basis in the Roth IRA.	Distributions come out of a Roth IRA in the following order. <ol style="list-style-type: none"> <li><b>Contributions:</b> Distributions are tax free and penalty free until total distributions exceed total contributions.</li> <li><b>Conversions and rollover contributions:</b> Distributions are tax free to the extent the amount was taxed upon conversion or rollover, plus any basis from nondeductible contributions.</li> <li><b>Earnings:</b> Distributions come from earnings only after all contributions and conversions are distributed.               <ul style="list-style-type: none"> <li>Qualified distributions are tax free and nonqualified distributions are taxable.<sup>2</sup></li> </ul> </li> </ol> See <i>Distributions</i> , page 13-12.	<ul style="list-style-type: none"> <li>New accounts can be set up any time by return due date, no extensions.</li> <li>Contributions must be made by the return due date, no extensions.</li> </ul>	<ul style="list-style-type: none"> <li>The 10% early withdrawal penalty may apply to distributions of earnings, unless exception applies.<sup>3</sup> Penalty never applies to distribution of contributions.</li> <li>The same 6% penalty on excess contributions that applies to traditional IRAs also applies to Roth IRAs if excess plus earnings are not withdrawn by due date (including extensions) of return. (IRC §4973)</li> </ul>
<b>SEP IRA</b> See page 13-13	<ul style="list-style-type: none"> <li>Must be self-employed or work as an employee for an employer that contributes to a SEP on behalf of all eligible employees.</li> <li>An employer cannot discriminate against any employee at least age 21 who has worked three of the immediately preceding five years for the employer with at least \$750 in compensation from the employer in 2024.</li> </ul>	<ul style="list-style-type: none"> <li>An employer must contribute a uniform percentage of pay for each eligible employee including those who die or terminate before contributions are made.</li> <li>An employer does not have to make contributions each year.</li> <li>Contributions must be based on a written allocation formula and must not discriminate in favor of highly-compensated employees.</li> <li>Contributions must be in the form of money.</li> </ul>	Contributions are generally deductible. Participation in another employer's pension does not affect the deduction. <b>Exception:</b> If a self-employed taxpayer contributes to a defined contribution plan, annual deductions are limited to the lesser of \$69,000 or 100% of the participant's compensation.	Distributions are subject to IRA rules. If the participant also has a nondeductible basis in a traditional IRA, distributions from a SEP IRA will be partially taxable and partially tax free as a return of basis.	<ul style="list-style-type: none"> <li>New accounts can be set up any time by return due date, including extensions.</li> <li>Contributions must be made by the return due date, including extensions.</li> </ul>	<ul style="list-style-type: none"> <li>10% penalty for early withdrawal unless exception applies.<sup>3</sup></li> <li>10% penalty on excess contributions. (IRC §4972 and IRC §4979)</li> <li>25% penalty for excess accumulation if required minimum distribution (RMD) rules are not followed. (IRC §4974)<sup>4</sup></li> </ul>

<sup>1</sup> For dollar limitations, see the *Pension Plan Limitations* chart, page 13-2

<sup>2</sup> [Reserved.]

<sup>3</sup> For exceptions to the 10% early withdrawal penalty, see *Exceptions to the 10% Penalty on Early Distributions* chart, page 13-3

<sup>4</sup> See *Required Minimum Distribution (RMD)*, page 13-21

## Pension Plan Characteristics — 2024 *continued*

	Qualifications	Contributions <sup>1</sup>	Deductions <sup>1</sup>	Distributions <sup>2</sup>	Due Dates	Penalties
<b>SIMPLE IRA</b> See page 13-14	Must be self-employed or work as an employee for a small employer that offers a SIMPLE plan. Employers cannot maintain any other pension plan and must have 100 or fewer employees who received at least \$5,000 of compensation for the preceding year.	<ul style="list-style-type: none"> <li>Each participant can decide the amount to contribute as an elective deferral, either as a percentage of compensation or a specific dollar amount.</li> <li>Employers must choose to either contribute matching amounts for participating employees, up to 3% of compensation (no limit), or choose nonelective contributions equal to 2% of compensation for all eligible employees (subject to annual compensation limit).</li> </ul> <p><b>New for 2024:</b> Increased amounts may apply in limited situations.</p>	Employee elective deferrals are generally excluded from the employee's income. Employer contributions (including self-employed deferrals and matching contributions) are generally deductible.	Distributions are subject to IRA rules. If the participant also has a nondeductible basis in a traditional IRA, distributions from a SIMPLE IRA will be partially taxable and partially tax free as a return of basis.	<ul style="list-style-type: none"> <li>New plan can be set up any time between January 1 and October 1 of year for which contributions will apply. Exception for new employers.</li> <li>Elective deferrals must be deposited into the employee's account within 30 days of the last day of the month in which the employee had the contribution withheld from wages.</li> <li>The employer must contribute the matching amounts by the return due date, including extensions. [IRC §408(p)(5)(A)]</li> </ul>	<ul style="list-style-type: none"> <li>10% penalty for early withdrawal unless exception applies.<sup>3</sup></li> <li>The early withdrawal penalty is increased to 25% if the withdrawal is within the first two years of establishing a SIMPLE plan. [IRC §72(t)(6)]</li> <li>10% penalty on excess contributions. (IRC §4972)</li> <li>25% penalty for excess accumulation if required minimum distribution (RMD) rules are not followed. (IRC §4974)<sup>4</sup></li> </ul>
<b>Qualified Plans</b> See page 13-16	<ul style="list-style-type: none"> <li>Self-employed individuals, partnerships, and corporations can set up qualified plans.</li> <li>All qualified plans must allow employees at least age 21 with at least one year of service (minimum of 1,000 hours) to be eligible for participation in the plan. [IRC §410(a)]</li> </ul> <p><b>Note:</b> Certain long-term part-time employees qualify to participate in 401(k) plans.</p>	Frequency and amount depends upon plan. Employee elective deferrals to 401(k) and 403(b) plans are at the discretion of the employee on a year-by-year basis. Employers are not required to match elective deferral contributions to 401(k) and 403(b) plans, except in the case of SIMPLE 401(k) and safe harbor 401(k) plans.	<ul style="list-style-type: none"> <li>Employee elective deferrals are generally excluded from the employee's income.</li> <li>Employer contributions (including self-employed deferrals and matching contributions) are generally deductible by the employer.</li> <li>Employee elective deferral limits apply to all plans of the participant.</li> </ul>	Distributions are fully taxable unless the employee or employer has contributed after-tax money to the plan. For rules, see <i>Cost basis in a retirement plan</i> , page 13-18.	<ul style="list-style-type: none"> <li>New plan must be set up by return due date, including extensions, of the year for which contributions will apply.</li> <li>Elective deferrals must be deposited into the employee's account no later than the 15th business day of the month following the payday.</li> <li>Employer contributions must be made by the return due date, including extensions. [IRC §404(a)(6)]</li> </ul>	<ul style="list-style-type: none"> <li>10% penalty for early withdrawal unless exception applies.<sup>3</sup></li> <li>10% penalty on excess contributions of employee elective deferrals and nondeductible employer contributions (IRC § 4972 and IRC §4979). Exception applies if excess deferrals are distributed within 2½ months of end of plan year.</li> <li>25% penalty for excess accumulation if required minimum distribution (RMD) rules are not followed. (IRC §4974)<sup>4</sup></li> </ul>

<sup>1</sup> For dollar limitations, see the *Pension Plan Limitations* chart, page 13-2

<sup>2</sup> [Reserved.]

<sup>3</sup> For exceptions to the 10% early withdrawal penalty, see *Exceptions to the 10% Penalty on Early Distributions* chart, page 13-3

<sup>4</sup> See *Required Minimum Distribution (RMD)*, page 13-21

## Pension Plan Advantages/Disadvantages—2024

	<i>Advantages:</i>		<i>Disadvantages:</i>	
<b>Traditional IRA</b> Page 13-7	<ul style="list-style-type: none"> <li>The participant is fully vested in the account at all times.</li> <li>The participant has complete control over allowable investment choices and decision making.</li> <li>Contributions provide for current year tax deductions.</li> <li>No annual reporting requirements.</li> <li>Does not reduce qualified business income (QBI).</li> </ul>	<ul style="list-style-type: none"> <li>Distributions may be used for qualified college expenses and first-time home purchases without the 10% early withdrawal penalty. These exceptions do not apply to other qualified pension plans.</li> <li><i>Deemed IRAs.</i> As part of an employer plan, the employee also has the convenience of having contributions made through payroll deductions.</li> </ul>	<ul style="list-style-type: none"> <li>The basis in a nondeductible traditional IRA must be mixed in with all other funds. The tax-free basis cannot be fully distributed until all funds in all traditional IRAs have been depleted.</li> <li>Taxpayers are required to begin distributions at age 73.</li> </ul>	<ul style="list-style-type: none"> <li>Deductible contributions are subject to phaseout rules for taxpayers who are also covered by an employer retirement plan.</li> <li>Contribution limits are generally lower than SIMPLE IRAs, SEPs, and other qualified plans.</li> </ul>
<b>Roth IRA</b> Page 13-11	<ul style="list-style-type: none"> <li>Qualified distributions, including tax-deferred earnings, can be withdrawn tax free.</li> <li>Distributions come from the taxpayer's basis before taxable earnings.</li> <li>The participant has complete control over investment choices and decision making.</li> </ul>	<ul style="list-style-type: none"> <li>Taxpayers are not required to begin distributions at age 73.</li> <li>AGI phaseout range is higher than for traditional IRAs.</li> <li>No annual reporting requirements.</li> <li><i>Deemed IRAs.</i> As part of an employer plan, the employee also has the convenience of having contributions made through payroll deductions.</li> </ul>	<ul style="list-style-type: none"> <li>No current tax deduction for contributions.</li> <li>Uncertainty over future tax law changes make future planning difficult and may make benefits less attractive than current tax deductions.</li> </ul>	
<b>SEP IRA</b> Page 13-13	<ul style="list-style-type: none"> <li>The participant is fully vested in the account at all times.</li> <li>Same tax deduction and deferral of income advantage as a traditional IRA.</li> <li>Employee can designate some or all elective deferrals as Roth (not excluded from income) that are generally subject to the same taxation under the Roth IRA rules.</li> </ul>	<ul style="list-style-type: none"> <li>Deductible contributions are not subject to AGI phaseout rules.</li> <li>Maximum contribution allowed for higher-income taxpayers is generally greater than an IRA.</li> <li>A SEP can be set up and deductible contributions made as late as the return due date, including extensions.</li> <li>No annual reporting requirements.</li> </ul>	<ul style="list-style-type: none"> <li>The employer must fund 100% of a participant's contribution. <b>Exception:</b> SARSEPs established prior to 1997.</li> <li>Low-income participants cannot contribute as much to a SEP IRA as they can to a traditional IRA or a SIMPLE IRA.</li> <li>Reduces qualified business income (QBI).</li> </ul>	
<b>SIMPLE IRA</b> Page 13-14	<ul style="list-style-type: none"> <li>The participant is fully vested in the account at all times.</li> <li>Same tax deduction and deferral of income advantage as a traditional IRA.</li> <li>Employee can designate some or all elective deferrals as Roth (not excluded from income) that are generally subject to the same taxation under the Roth IRA rules.</li> <li>Maximum contribution allowed is generally greater than an IRA.</li> <li>Lower-income taxpayers can contribute a higher percentage of earnings than a SEP.</li> </ul>	<ul style="list-style-type: none"> <li>No annual reporting requirements.</li> <li>Similar features of a 401(k) plan without the complexity and restrictions placed on highly-compensated employees.</li> <li>Elective deferrals through payroll withholding make it easier for employees to save for retirement.</li> <li>Unlike a SEP IRA, most of the funds are contributed by the employee through voluntary elective deferrals. The employer match is relatively small in comparison.</li> </ul>	<ul style="list-style-type: none"> <li>Must be set up by October 1 of the year contributions are to apply.</li> <li>Employer with over 100 employees cannot have a SIMPLE IRA.</li> <li>Lower elective deferral limits than 401(k) plans.</li> </ul>	
<b>401(k) Plan</b> Page 13-16	<ul style="list-style-type: none"> <li>The participant is fully vested in elective deferrals at all times.</li> <li>Same tax deduction and deferral of income advantage as a traditional IRA.</li> <li>Employee can designate some or all elective deferrals as Roth (not excluded from income) that are generally subject to the same taxation under the Roth IRA rules.</li> <li>Maximum contribution allowed is generally greater than an IRA.</li> </ul>	<ul style="list-style-type: none"> <li>Elective deferral limits greater than SIMPLE IRAs.</li> <li>Employers often match dollar-for-dollar employee elective deferrals up to certain percentages.</li> <li>Plan participants may choose to receive employer matching and nonelective contributions as Roth contributions.</li> <li>Elective deferrals through payroll withholding makes it easier for employees to save for retirement.</li> </ul>	<ul style="list-style-type: none"> <li>Complexity and restrictions placed on highly-compensated employees make it difficult and sometimes expensive to administer.</li> <li>Key employees do not always receive the full benefit of allowable elective deferrals.</li> </ul>	
<b>403(b) Tax-Sheltered Annuity Plan</b> Page 13-17	<ul style="list-style-type: none"> <li>The participant is fully vested in elective deferrals at all times.</li> <li>Same tax deduction and deferral of income advantage as a traditional IRA.</li> <li>Employee can designate some or all elective deferrals as Roth (not excluded from income) that are generally subject to the same taxation under the Roth IRA rules.</li> </ul>	<ul style="list-style-type: none"> <li>Elective deferral limits greater than SIMPLE IRAs.</li> <li>Employers often match dollar-for-dollar employee elective deferrals up to certain percentages.</li> <li>Elective deferrals through payroll withholding make it easier for employees to save for retirement.</li> </ul>	<ul style="list-style-type: none"> <li>Limited as to what types of employers are eligible to offer a 403(b) plan to employees. Generally available only for employees of certain tax-exempt organizations.</li> </ul>	
<b>Defined Contribution Plan</b> Page 13-16	<ul style="list-style-type: none"> <li>Same tax deduction and deferral of income advantage as a traditional IRA.</li> </ul>	<ul style="list-style-type: none"> <li>Maximum contribution allowed for higher-income taxpayers is generally greater than an IRA.</li> <li>Deductible contributions are not subject to AGI phaseout rules.</li> </ul>	<ul style="list-style-type: none"> <li>Can be more expensive and difficult to administer than a SEP or SIMPLE plan.</li> <li>Annual reports are generally required.</li> </ul>	<ul style="list-style-type: none"> <li>Future benefits are dependent on contributions and fund performance.</li> </ul>
<b>Defined Benefit Plan</b> Page 13-16	<ul style="list-style-type: none"> <li>Designed to provide a guaranteed monthly benefit for the life of a participant.</li> <li>Shareholder employees of closely held corporations can contribute and deduct more per year to a defined benefit plan than a defined contribution plan. Contributions for self-employed taxpayers are limited to 100% of compensation per year. [IRC §404(a)(8)]</li> </ul>		<ul style="list-style-type: none"> <li>Fixed income could be inadequate in future years as inflation decreases the defined benefit.</li> </ul>	
<b>Nonqualified Deferred Compensation Plan</b> Page 13-19	<ul style="list-style-type: none"> <li>The plan can discriminate in favor of key employees and owners.</li> <li>There are no contribution limits or funding requirements.</li> </ul>		<ul style="list-style-type: none"> <li>In order for an employee to defer taxes on the benefit, the employee has to be at risk for forfeiting the funds in the account through various contingencies. There is no minimum funding or vesting rules to protect employees.</li> <li>Employer receives no benefit from a tax deduction for contributions until the contributions are reportable in the employee's Form W-2 wages.</li> <li>Plan earnings are generally not tax deferred.</li> </ul>	

# Individual Retirement Arrangement (IRA)

## Cross References

- IRS Pub. 590-A, *Contributions to Individual Retirement Arrangements (IRAs)*
- IRS Pub. 590-B, *Distributions from Individual Retirement Arrangements (IRAs)*
- IRC §219, *Retirement savings*
- IRC §408, *Individual retirement accounts*

## Related Topics

- Retirement Savings Contributions Credit, page 11-16

### IRA Limits—2024

Individual Contribution Combined Limit—Traditional and Roth IRAs	
Under age 50.....	\$7,000
Age 50 or older.....	\$8,000

#### Traditional IRA Phaseouts

Taxpayer is covered by an employer retirement plan:

MFJ, QSS	Single, HOH	MFS
\$123,000 to \$143,000	\$77,000 to \$87,000	\$0 to \$10,000

Contributing spouse is not covered by an employer retirement plan but other spouse is:

MFJ	MFS
\$230,000 to \$240,000	\$0 to \$10,000

See *Reduced IRA Deduction*, page 13-9.

## Who Can Set Up a Traditional IRA?

A traditional IRA is any IRA that is not a Roth IRA or a SIMPLE IRA. Any individual can set up a traditional IRA if he or she receives taxable compensation during the year. An individual can have a traditional IRA even if covered by an employer-sponsored retirement plan. However, the deductible amount of contributions to a traditional IRA may be phased out. See *Reduced IRA Deduction*, page 13-9.

**Contribution limit.** Contributions to IRAs are limited to the lesser of the individual's compensation (or spouse's compensation under a spousal IRA), or \$7,000 (\$8,000 age 50 or older). Total contributions are combined with Roth IRA contributions to determine limits. For example, a \$1,000 contribution to a Roth IRA will reduce total contributions allowable to a traditional IRA by \$1,000. Employer contributions, including elective deferrals, under a SEP IRA or SIMPLE IRA plan do not affect this limit. See *Pension Plan Limitations* chart, page 13-2.

**New for 2024** The additional \$1,000 catch-up contribution for individuals age 50 or older is now indexed for inflation.

**Age limit for contributions.** Taxpayers can make qualified contributions to an IRA at any age.

**Brokers' commissions.** Commissions paid in connection with an IRA are considered to be a part of the contribution that is subject to the limits.

**Trustee fees.** Fees paid to administer the IRA are not considered to be part of the contribution. Trustee fees billed separately and paid from funds not inside the IRA are not deductible.

**Spousal IRA.** If both spouses have compensation, each can set up a separate IRA. Spouses cannot participate in the same IRA. However, if MFJ, and one spouse's compensation is less than the contribution limit, the lower-income spouse can use the compensation of the other spouse to qualify as only one spouse needs to have compensation.

**Example #1:** Jill is a full-time student under age 50 with no taxable compensation. Her husband, Barry, is under age 50 and has taxable compensation of \$30,000. If they file a joint return, Barry and Jill can each contribute \$7,000 in 2024 to their own IRAs.

**Example #2:** Assume the same facts as Example #1, except that Barry's taxable compensation is only \$7,500. Barry contributes \$7,000 to his IRA. Jill's IRA contribution is limited to \$500.

**Contribution deadline.** A contribution can be made for a year at any time during the year, up to the due date for filing the tax return for that year, not including extensions. For contributions that apply to tax year 2024, the deadline for making the contribution is April 15, 2025. Contributions do not have to be made each and every year, even if the participant qualifies to make a contribution.

If a contribution is mailed to the IRA trustee, the post office cancellation mark is considered the date the contribution is made if the trustee receives the contribution after the due date of the return. (Ltr. Rul. 8536085)

**Designating year.** Contributions made between January 1 and April 15, 2025, can apply to either 2024 or 2025. If the trustee is not informed which year to designate the contribution to, the trustee can assume it is for the current year (the year received). The tax return can be filed prior to actually making the contribution, as long as it is contributed by the due date of the return, not including extensions.

**Advantages/disadvantages.** See the *Pension Plan Advantages/Disadvantages* chart, page 13-6.

**SEP IRA.** A SEP is a written arrangement that allows an employer to make deductible contributions to a traditional IRA set up for an employee. Distributions are generally subject to the same rules that apply to traditional IRAs. See *Simplified Employee Pension (SEP)*, page 13-13.

## Compensation for IRA Contribution Purposes

For purposes of contributing to an IRA, compensation is earnings from work, whether as an employee or self-employed. Compensation includes the following types of income.

- Wages, salaries, tips, professional fees, bonuses, commissions, military differential pay, and any other taxable amounts included in box 1, Form W-2, (e.g., scholarships, fellowships, and stipends).
- Net earnings from self-employment as a sole proprietor or a partner of a partnership, reduced by the deduction for one-half of self-employment (SE) tax and any deductions for contributions to a qualified retirement plan. Net SE earnings also include income not subject to SE tax due to a religious election to be excluded from Social Security coverage.
- Taxable alimony and separate maintenance payments received under a decree of divorce or separate maintenance.
- Nontaxable combat pay (code Q, box 12, Form W-2).
- Taxable non-tuition fellowship and stipend payments made to aid the taxpayer in the pursuit of graduate or postdoctoral study and included in his or her gross income.

Compensation does not include the following types of income.

- Earnings and profits from property, such as rental, interest, and dividend income.
- Pension or annuity income.
- Deferred compensation from a previous year.
- Partnership income if the partner did not provide services that are a material income-producing factor.
- Conservation Reserve Program (CRP) payments reported on line 1b, Schedule SE (Form 1040).
- Any amounts (except combat pay) excluded from income, such as income qualifying for the foreign earned income exclusion, fringe benefits, and nontaxable scholarships.

## IRA Investment

An IRA can be invested in a variety of different products, such as products offered by banks, mutual funds, brokerage companies,

life insurance companies, or other financial institutions. The IRA is a trust or custodial account set up for the exclusive benefit of the participant and the beneficiary.

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**Author's Comment:** Every IRA must be maintained by a trustee or custodian separate from the participant and beneficiary. Thus, the kind of investment an IRA can be invested in depends upon whether an IRA trustee agrees to manage a particular investment. For example, using IRA funds to purchase privately held stock (stock that is not traded on an open market such as the New York Stock Exchange) would require having an IRA trustee take possession of the stock certificates until they are sold. A taxpayer cannot buy, take possession of, and then sell stock on behalf of his or her own IRA. However, this does not mean the participant cannot self-direct purchases and sales. Most online brokerage companies allow investors to directly buy and sell stock in their IRAs as long as the brokerage firm, as the trustee, maintains possession of the stock while held in the IRA.

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## Prohibited Transactions Involving IRAs

Penalties apply when IRA funds are used in prohibited transactions. A prohibited transaction is any improper use of traditional IRA funds by the participant, the beneficiary, or a disqualified person. The following are examples of prohibited transactions.

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

**Prohibited transaction penalty.** A prohibited transaction causes the IRA to stop being an IRA as of the first day of the year in which a prohibited transaction occurs. The FMV of the account is treated as being distributed to the participant on the first day of the year.

**Involved IRA.** If an individual has multiple IRAs, only the IRA for which the prohibited transaction occurred will be disqualified.

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**Author's Comment:** Occasionally, taxpayers consider purchasing land with IRA funds. If a trustee can be found who is willing to hold and manage the land in an IRA, the land could qualify as a proper investment for the IRA. However, if the taxpayer ever visits the land for personal use, or has the intention of building a residence on it some day, such use would be considered a prohibited transaction.

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## Investment in Collectibles

An IRA cannot invest in collectibles, such as artwork, rugs, antiques, metals, gems, stamps, coins, or alcoholic beverages. If an IRA invests in collectibles, the amount invested is considered distributed in the year invested and the taxpayer may be subject to the 10% early distribution penalty.

**Exception:** An IRA can invest in one, one-half, one-quarter, or one-tenth ounce U.S. gold coins or one-ounce silver coins minted by the Treasury Department. It can also invest in certain platinum coins and certain gold, silver, palladium, and platinum bullion.

## IRA Distributions

**Reporting.** IRA distributions and pension and annuity distributions are reported on separate lines on Form 1040. Lines 4a and 4b are used to report IRA distributions. Lines 5a and 5b are used to report pension and annuity income.

**Taxable distribution.** In general, a distribution from a traditional IRA is taxable in the year received unless it is a rollover, qualified charitable distribution, qualified HSA funding distribution, or a return of nondeductible contributions. See *Rollovers and Transfers*, page 13-19, *Qualified charitable distribution (QCD)*, Tab 4, and *Qualified HSA Funding Distribution (QHFD)*, page 13-24.

**Age 59½ rule.** A taxpayer can withdraw from a traditional IRA at any time, however, a 10% early withdrawal penalty tax applies if the taxpayer is under age 59½. The 10% additional tax applies to the part of the distribution included in gross income. See *Exceptions to the 10% Penalty on Early Distributions*, page 13-3.

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**Author's Comment:** There are exceptions to the 10% early distribution penalty for withdrawals from an IRA for a first-time home purchase, education funding, and purchase of health insurance. These exceptions do not apply to early distributions from employer and 401(k) plans. The penalty on early withdrawal from a 401(k) or employer plan could be avoided by first rolling the distribution over, if allowed by the plan, to an IRA.

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**Taxable amount of distribution.** Distributions from a traditional IRA may be fully or partly taxable, depending on whether the IRA includes any nondeductible contributions (cost basis). See *Nondeductible Contributions to IRAs*, page 13-11.

If only deductible contributions were made to traditional IRA(s), the taxpayer has no basis in the IRA(s) and a distribution is fully taxable as ordinary income. If nondeductible contributions were made or any after-tax amounts were rolled over to any traditional IRA, a distribution from any traditional IRA will be partly taxable and partly a return of cost basis. The taxpayer cannot choose to have the cost basis distributed first. The values of all traditional IRAs are aggregated to determine the taxable portion of a distribution. Use Form 8606, *Nondeductible IRAs*, to compute the taxable and nontaxable portion of a distribution.

**Proof of cost basis.** Tax records should be kept for all years in which nondeductible IRA contributions were made. Without such proof, the IRS can deny the cost basis and subject the entire distribution to taxation. (*Alpern*, T.C. Memo. 2000-246)

**Form 5498, IRA Contribution Information.** Form 5498 provides the IRS and recipients information on contributions, rollovers, conversions, recharacterizations, and the fair market value (FMV) of the account at the end of the year. The FMV information is needed for purposes of the required minimum distribution (RMD) rules and in computing the taxable and nontaxable portion of an IRA distribution.

**Losses.** Losses on traditional IRAs and Roth IRAs are not deductible.

## Excess IRA Contributions

### Cross References

- Form 5329, *Additional Taxes on Qualified Plans (Including IRAs) and Other Tax-Favored Accounts*
- IRS Pub. 590-A, *Contributions to Individual Retirement Arrangements (IRAs)*
- IRS Pub. 590-B, *Distributions from Individual Retirement Arrangements (IRAs)*

### Related Topics

- Exceptions to 10% Additional Tax—Education, page 12-6
- Excess contribution penalty, page 29-15

• **Note:** A taxpayer who has not made an excess contribution, but simply has changed his or her mind, can also use these rules to withdraw all or a portion of a contribution made during the year.

### Excess Contribution Excise Tax Penalty

An excess contribution results when a taxpayer has contributed more than the annual limit to a traditional IRA or a Roth IRA. See the *Pension Plan Limitations* chart, page 13-2.

If any part of the excess contribution is allowed to remain in the IRA past the due date for correcting the excess, it is subject to



a 6% excise tax. The 6% penalty applies each year the excess is allowed to remain in the IRA. Use Form 5329, *Additional Taxes on Qualified Plans (Including IRAs) and Other Tax-Favored Accounts*, to calculate the penalty.

**Other excess contributions subject to the 6% penalty.** In addition to excess contributions to IRAs, this same penalty (and procedure for avoiding the penalty) applies to excess contributions to Coverdell ESAs, Archer MSAs, ABLE accounts, and HSAs.

### How to Correct an Excess Contribution

If an excess contribution is made during the year, the excess contribution penalty will not apply if the excess is withdrawn by the due date for filing the return, including extensions. The withdrawal is considered a tax-free distribution if:

- The taxpayer does not take a deduction for the contribution, and
- The taxpayer withdraws any interest or other income earned on the contribution while it was part of the IRA. For this purpose, any loss on the contribution is also taken into consideration when calculating the amount to withdraw.

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**Author's Comment:** The taxpayer's broker typically calculates the amount of earnings on excess contributions (versus a calculation by the tax preparer using the worksheet)

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If necessary, use the worksheet, below, to calculate the net income or loss on the excess contribution.

#### Net Income Worksheet for Recharacterizations and Excess Contributions

Use this worksheet to determine the income on IRA contributions that are being recharacterized or the income on excess IRA contributions that must be distributed along with the excess contributions.

- 1) Enter amount of IRA that is being recharacterized or the excess amount being distributed..... 1) \_\_\_\_\_
- 2) Enter FMV of the IRA immediately prior to the recharacterization or distribution of excess contributions. Include any distributions, transfers, or recharacterizations made while the contribution was in the account.. 2) \_\_\_\_\_
- 3) Enter FMV of the IRA immediately prior to the time the contribution being recharacterized was made or excess contribution being distributed was made, including the amount of such contribution and any other contributions, transfers, or recharacterizations made while the contribution was in the account..... 3) \_\_\_\_\_
- 4) Subtract line 3 from line 2 (can be negative)..... 4) \_\_\_\_\_
- 5) Divide line 4 by line 3. Enter the result as a decimal. Round to at least three places (can be a negative fraction)..... 5) \_\_\_\_\_
- 6) Multiply line 1 by line 5. This is the net income (or loss) attributable to the contribution that is being recharacterized or the excess contribution being distributed..... 6) \_\_\_\_\_
- 7) Add line 1 and line 6. This is the amount of the IRA contribution plus the net income (or loss) attributable to it to be recharacterized or excess contribution being distributed. 7) \_\_\_\_\_

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**Example:** On May 1, 2024, when her IRA is worth \$4,800, Kelly (age 29) makes a \$1,600 contribution to her traditional IRA. On February 1, 2025, when she files her 2024 tax return, she discovers that her total compensation for the year is only \$1,200. Her May 1, 2024 contribution exceeded her limit by \$400. Her IRA is worth \$7,600 on February 1, 2025, when she directs her IRA trustee to distribute the \$400 excess contribution plus net income attributable to the excess contribution. No other IRA contributions or distributions were made during 2024. Using the *Net Income Worksheet for Recharacterizations and Excess Contributions*, above, the amounts to enter on each line are as follows: Line 1 = \$400, line 2 = \$7,600, line 3 = \$6,400, line 4 = \$1,200, line 5 = 0.1875, line 6 = \$75, and line 7 = \$475.

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**How to treat withdrawn interest or other income.** The taxpayer must include in his or her gross income the interest or other income that was earned on the excess contribution for the year in which the excess contribution was made. The 10% additional penalty tax does not apply to a corrective IRA distribution (withdrawal of excess contribution plus any earnings) made on or before the due date (including extensions) of the tax return.

**Last-in, first-out rule.** If more than one contribution is made during the year, the last contribution is considered to be the one that is withdrawn first for purposes of calculating net income on earnings.

### Excess Contribution Withdrawn After Due Date for the Return

If the excess contribution is withdrawn after the due date (or extended due date), the distribution is generally taxable. However, the distribution is not taxable if both of the following conditions are met.

- Total contributions (other than rollover contributions) for 2024 were not more than \$7,000 (\$8,000 if age 50 or older), and
- Taxpayer did not take a deduction for the excess contribution being withdrawn.

The withdrawal can take place at any time, even after the due date, including extensions, for filing the tax return.

**Form 1040-X, Amended U.S. Individual Income Tax Return.** A taxpayer can treat the excess as not being deducted by filing Form 1040-X and removing the deduction for the excess contribution on the amended return.

### Deducting an Excess Contribution in a Later Year

Another way to handle an excess contribution is to pay the 6% excise tax penalty on the excess and leave it in the IRA. In the following year, undercontribute to the IRA for that year and apply the prior year excess contribution to the current year contribution. If the excess contribution carryover still exceeds the contribution allowed for that year, pay the 6% penalty on the difference and carry the remainder over to the next year. Keep doing this until the excess is used up.

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**Example:** Kathy made a contribution to her IRA for 2023 in the amount of \$6,500. An unexpected medical issue caused a disability for Kathy early in the year, leaving her compensation for purposes of an IRA contribution at only \$4,350. Kathy had an excess contribution for 2023 in the amount of \$2,150 (\$6,500 – \$4,350). She did not withdraw the excess contribution by the due date of the return including extensions. For 2023, Kathy paid the penalty for allowing the excess contributions to remain in her IRA in the amount of \$129 (\$2,150 × 6%).

In 2024, Kathy earned \$2,800 at a part-time job. Since she had not withdrawn the excess contribution from 2023, Kathy is able to apply the \$2,150 excess contribution from 2023 as an allowable contribution for 2024. There is no penalty in 2024 for an excess contribution.

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## Reduced IRA Deduction

### Cross References

- Form 8606, *Nondeductible IRAs*
- IRS Pub. 590-A, *Contributions to Individual Retirement Arrangements (IRAs)*
- IRS Pub. 590-B, *Distributions from Individual Retirement Arrangements (IRAs)*
- IRC §219(g), *Limitation on deduction for active participants in certain pension plans*

### Related Topics

- IRA Based Plans, page 29-7
- Qualified Plans, page 29-11

**Note:** If neither the taxpayer nor spouse was covered for any part of the year by an employer retirement plan, the following phaseout rules do not apply. Deduct the total IRA contributions for the year up to the annual limits. See *IRA Limits—2024*, page 13-7.

### Phaseout Based on Modified AGI (MAGI)

If an individual is covered by an employer retirement plan or through self-employment, the deduction for an IRA contribution decreases (phases out) when MAGI is between the following amounts. See *Modified Adjusted Gross Income (MAGI)*, next column.

Tax Year	MFJ, QSS	Single, HOH	MFS
2024	\$123,000 to \$143,000	\$77,000 to \$87,000	\$0 to \$10,000

For tax years 2019–2024 limits see *Retirement Plan Limits*, page 1-3.

If a married individual is not covered, but his or her spouse is, the non-covered spouse's deduction is phased out when modified AGI is between the following amounts.

Tax Year	MFJ	MFS
2024	\$230,000 to \$240,000	\$0 to \$10,000

For tax years 2020–2025 limits see *Retirement Plan Limits*, page 1-3.

Nondeductible contributions are added to the taxpayer's basis in the IRA.

**Married Filing Separately (MFS).** For purposes of the deduction phaseout ranges, MFS assumes both spouses live together. If spouses lived apart during the entire year and file MFS, they are considered Single for purposes of the phaseout rules.

**Spousal IRA.** If an individual uses the income of a spouse to qualify for an IRA deduction (spousal IRA), the individual is not considered covered by an employer retirement plan, even if the spouse whose income is used to qualify is covered. In that case, the \$230,000 to \$240,000 (for 2024) phaseout rules apply. [IRC §219(g)(7)]

### IRA Deduction Phaseout Worksheet

If MAGI is within the phaseout range, use the following worksheet to calculate the deductible and nondeductible portion of the contribution. Each spouse should fill out a separate worksheet. This worksheet is designed to work for all years. For example, use it to plan for estimated tax purposes in the following year.

- 1) Enter ending phaseout amount based on filing status and tax year. See phaseout ranges, above. For example, phaseout for MFJ in 2024 ends at \$143,000 ..... 1) \_\_\_\_\_
- 2) Enter MAGI (for both spouses if MFJ) ..... 2) \_\_\_\_\_
- 3) Subtract line 2 from line 1 ..... 3) \_\_\_\_\_
- 4) Divide the maximum IRA contribution allowed by the size of the phaseout range. For example, MFJ, 2024, taxpayer under age 50 =  $\$7,000 \div \$20,000 = 35\%$  ..... 4) \_\_\_\_\_
- 5) Multiply line 3 by percentage on line 4. If the result is not a multiple of \$10, round to the next highest multiple of \$10. For example, \$611 is rounded to \$620. If result is less than \$200, enter \$200 ..... 5) \_\_\_\_\_
- 6) Enter compensation minus the sum of the deductions for one-half SE tax, SEP, SIMPLE, or qualified plan contributions. If MFJ and compensation is less than spouse's compensation, use spouse's compensation reduced by his or her traditional IRA and Roth IRA contributions. Do not reduce compensation by losses from self-employment ..... 6) \_\_\_\_\_
- 7) Enter IRA contributions for the year, but do not exceed the IRA contribution limit for the year ..... 7) \_\_\_\_\_
- 8) **IRA deduction.** Enter the smallest of lines 5, 6, or 7, or a smaller amount if chosen ..... 8) \_\_\_\_\_
- 9) **Nondeductible contribution.** If line 7 is more than line 8, subtract line 8 from line 6 or 7, whichever is smaller. Enter here and on Form 8606, *Nondeductible IRAs* ..... 9) \_\_\_\_\_

### Modified Adjusted Gross Income (MAGI)

For purposes of the IRA deduction phaseout, MAGI equals AGI without taking into account any IRA deduction, plus the sum of the following.

- Student loan interest deduction.
- Foreign earned income exclusion.
- Foreign housing exclusion or deduction.
- Excluded U.S. Savings Bond interest, used for education.
- Excluded employer-provided adoption benefits.

**Both contribution and distribution in same year.** If a taxpayer received a distribution from an IRA and made an IRA contribution in the same year, the taxable part of the distribution must be calculated prior to determining MAGI for purposes of the phaseout rules. See IRS Pub. 590-B for Worksheet 1-1, *Figuring the Taxable Part of Your IRA Distribution*.

**Social Security recipients.** A special computation is required if all the following apply.

- Taxpayer received Social Security benefits during the year,
- Taxpayer received taxable compensation during the year,
- Contributions were made to the taxpayer's traditional IRA during the year, and
- Taxpayer or spouse was covered by an employer-sponsored retirement plan.

If all of the above apply, use the following steps to compute taxable Social Security and the deductible IRA contribution.

- 1) Compute taxable Social Security as if no IRA deduction was taken.
- 2) Compute the IRA deduction using the *IRA Deduction Phaseout Worksheet*, previous column, with taxable Social Security calculated in step one.
- 3) Re-compute taxable Social Security using the IRA deduction from step two.

If the foreign earned income exclusion, foreign housing deduction or exclusion, U.S. possessions income exclusion, Puerto Rico income exclusion, or exclusion for employer-paid adoption expenses apply, use the worksheets in Appendix B in IRS Pub. 590-A to compute the deductible amount, the nondeductible contribution, and the taxable portion, if any, of the Social Security benefits.

### Covered By an Employer Retirement Plan

If an employee is covered by an employer retirement plan, box 13 of Form W-2 should have the retirement plan box checked.

An employee is covered by an employer retirement plan for a tax year if the employer has a:

- Defined contribution plan [profit-sharing, 401(k), stock bonus, or money purchase pension plan] and any contributions or forfeitures are allocated to the employee's account for the tax year.
- IRA-based plan (SEP, SARSEP, or SIMPLE IRA) and the employee has an amount contributed to the IRA for the tax year.
- Defined benefit plan [403(b) annuity, cash balance, or plans for federal, state, or local government employees, other than section 457(b) plans] and the employee is eligible to participate within the tax year. An employee is covered even if he or she declines to participate, does not make a required contribution, or does not perform the minimum service required to accrue a benefit for the year.

**No vested interest.** If any amount is allocated to or a benefit accrues to an employee's account, the employee is covered by that plan even if he or she has no vested interest in (legal right to) the account.

**Court Case:** The taxpayer was a part-time employee of a public school and was automatically enrolled in a statewide employer-sponsored qualified defined benefit plan. She was required to contribute \$84.89 to the plan on \$2,830 of compensation, which qualified her 0.083 years of service credit during the year. At that rate, she would have had to work

for 120 years to accumulate the minimum 10 years of credited service to qualify for benefits. The court ruled she was covered by an employer plan and denied her IRA deduction for the year. (*Wade*, T.C. Memo. 2001-114)

**Not covered.** An employee is not considered covered by an employer retirement plan under any of the following.

- Participation in a nonqualified deferred compensation plan, including a section 457(b) plan.
- Coverage under Social Security or railroad retirement.
- The mere act of receiving benefits under a previous employer's pension plan.
- Plan of the United States, a state, or political subdivision of a state for a reservist who does not serve more than 90 days on active duty (not counting training) during the year.
- Plan of the United States, a state, or political subdivision of a state for a volunteer firefighter where accrued benefits at the beginning of the year will not provide more than \$1,800 per year at retirement.

### Nondeductible Contributions to IRAs

If a taxpayer cannot deduct all or a portion of an allowable IRA contribution, the taxpayer can choose to make a nondeductible contribution. IRA contribution limits still apply.

**Form 8606, Nondeductible IRAs.** To designate contributions as nondeductible, file Form 8606. Contributions that are otherwise deductible can be designated as nondeductible if the taxpayer chooses to do so. As long as the nondeductible contributions are in the IRA, the earnings on the contributions are not taxed until distributed.

**Note:** Contributions not reported as nondeductible on Form 8606 are treated as deductible even though a deduction was not taken or not allowed on the tax return. All future distributions from the taxpayer's IRAs will be treated as taxable distributions unless evidence can be produced showing nondeductible contributions were made.

**Author's Comment:** There is no statute of limitations on the filing of Form 8606 however a \$50 penalty may apply for failure to file. If the taxpayer is not required to file an income tax return, Form 8606 can be filed on its own.

**Cost basis.** Nondeductible contributions will produce a cost basis in the IRA. The cost basis of an IRA equals total nondeductible contributions minus total withdrawals of nondeductible contributions. The cost basis of all the taxpayer's IRAs is recorded on Form 8606. The taxable and nontaxable portion of a distribution is also computed on Form 8606. See *IRA Distributions*, page 13-8.

## Roth IRA

### Cross References

- IRS Pub. 590-A, *Contributions to Individual Retirement Arrangements (IRAs)*
- IRS Pub. 590-B, *Distributions from Individual Retirement Arrangements (IRAs)*
- IRS Pub. 4530, *Designated Roth Accounts Under 401(k), 403(b), or Governmental 457(b) Plans*
- IRC §408A, *Roth IRAs*

### Related Topics

- Retirement Savings Contributions Credit, page 11-16
- Qualified Tuition Programs (QTPs) and Education Savings Accounts (ESAs), page 12-5
- Small Business Retirement, Tab 29

### Roth IRA Limits—2024

#### Individual Contribution Combined Limit—Traditional and Roth IRAs

Under age 50.....	\$7,000
Age 50 or older.....	\$8,000

#### Roth IRA Phaseouts

MFJ or QSS.....	\$230,000–\$240,000
Single, HOH, or MFS (lived apart from spouse all year).....	\$146,000–\$161,000
MFS (lived with spouse at any time during the year)	\$0–\$10,000

### Roth IRA Rules

A Roth IRA is subject to the same rules as a traditional IRA except:

- Contributions are not deductible. Thus, being covered by an employer retirement plan is irrelevant.
- If certain requirements are satisfied, distributions are tax free. For details, see *Distributions*, page 13-12.
- The required minimum distribution (RMD) rules do not apply. Distributions are not required until the death of the participant.
- Contributions phase out. See *Roth IRA Phaseouts*, above.

**Modified AGI.** Modified AGI for Roth IRA purposes is AGI minus conversion income (any income resulting from the conversion or rollover from a qualified retirement plan to a Roth IRA).

To the resulting amount add the following.

- Traditional IRA deduction.
- Student loan interest deduction.
- Foreign earned income exclusion.
- Foreign housing exclusion or deduction.
- Excluded U.S. Savings Bond interest used for education.
- Excluded employer-provided adoption benefits.

**Contribution limit.** Contributions to a Roth IRA are limited to the lesser of the taxpayer's compensation (or spouse's compensation under a spousal Roth IRA), or \$7,000 (\$8,000 age 50 or older). Total contributions are combined with traditional IRA contributions to determine limits. For example, a \$1,000 contribution to a traditional IRA will reduce total contributions allowable to a Roth IRA by \$1,000. Employer contributions, including elective deferrals, under a SEP IRA or SIMPLE IRA plan do not affect this limit. See *Pension Plan Limitations* chart, page 13-2.

**Spousal Roth IRA.** The rules for spousal Roth IRAs are the same as for traditional IRAs. See *Spousal IRA*, page 13-10.

**Military death benefit.** Taxpayers receiving a military death gratuity or Servicemembers' Group Life Insurance (SGLI) payment can contribute (roll over) all or part of the amount received to a Roth IRA. The contribution is treated as a qualified rollover contribution that is not taxable. The amount contributed cannot exceed the total amount received reduced by any part of that amount that was contributed to a Coverdell ESA or another Roth IRA. Any military death gratuity or SGLI payment contributed to a Roth IRA is disregarded for purposes of the one-year waiting period between rollovers. The contribution cannot be made later than one year after the date the taxpayer received the payment. The amount contributed to the Roth IRA is treated as part of the cost basis in the Roth IRA that is not taxable when distributed.

### Roth IRA Contribution Phaseout Worksheet for 2024

Use if the taxpayer's modified AGI falls within the phaseout range for making Roth IRA contributions. See *Modified AGI*, above.

- |  |          |
|--|----------|
| 1) Enter modified AGI for Roth IRA purposes.....   | 1) _____ |
| 2) Enter \$230,000 if MFJ or QSS, \$0 if MFS (and lived with spouse at any time during the year), or \$146,000 for all others..... | 2) _____ |
| 3) Subtract line 2 from line 1.....  | 3) _____ |

*continued on next page*

- 4) Enter \$10,000 if MFJ, QSS, or MFS (and lived with spouse at any time during the year), or \$15,000 for all others ..... 4) \_\_\_\_\_
- 5) Divide line 3 by line 4 and enter the result as a decimal, rounded to at least three places, but not more than 1.000..... 5) \_\_\_\_\_
- 6) Enter the lesser of the maximum Roth IRA contribution allowed for the year (see page 13-11) or taxable compensation ..... 6) \_\_\_\_\_
- 7) Multiply line 5 by line 6 ..... 7) \_\_\_\_\_
- 8) Subtract line 7 from line 6. Round the result up to the nearest \$10. If the result is less than \$200, enter \$200... 8) \_\_\_\_\_
- 9) Enter contributions for the year to other IRAs..... 9) \_\_\_\_\_
- 10) Subtract line 9 from line 6..... 10) \_\_\_\_\_
- 11) Enter the lesser of line 8 or line 10. This is the reduced Roth IRA contribution limit..... 11) \_\_\_\_\_

## Distributions

Do not include in gross income any Roth IRA distribution that is a qualified distribution, a return of regular contributions, or that is rolled over into another Roth IRA. Only nonqualified distributions are taxable.

**Ordering rules.** Roth IRAs are distributed in the following order:

- 1) **Regular contributions.** Distributions of regular contributions are tax and penalty free and can be withdrawn at any time.
- 2) **Conversion and rollover contributions.** Distributions are taken on a first-in, first-out basis, and are tax-free to the extent the amount was taxed upon conversion or rollover, plus any basis from nondeductible contributions. Take the taxable portion into account first, and then the nontaxable portion. See *Conversion Rules*, next column. See *Rollovers and Transfers*, page 13-19.
- 3) **Earnings on contributions.** Distributions come from earnings only after all contributions, conversions, and rollovers are distributed.

**Qualified distribution.** A qualified distribution is tax-free if the taxpayer has held a Roth IRA for five years and the distribution is:

- Made on or after the date the taxpayer reaches age 59½, or
- Made due to the taxpayer's death or disability, or
- For a qualified first-time home purchase (\$10,000 lifetime limit).

**Nonqualified distribution.** A nonqualified distribution is taxable and the 10% early withdrawal penalty applies to the taxable portion of the distribution unless an exception applies. See *Exceptions to the 10% Penalty on Early Distributions* chart, page 13-3.

To compute the taxable part of a distribution, complete Part III, Form 8606, *Nondeductible IRAs*.

**Example:** In 2021, Jerry, age 40, converted his \$10,000 traditional IRA to a Roth IRA and included the entire amount in his income for the year. In 2022 and 2023, Jerry contributed \$4,000 to his Roth IRA for a total of \$8,000 in regular contributions.

In 2024, Jerry withdrew \$20,000 from his Roth IRA. The first \$8,000 of the distribution is a return of Jerry's regular contributions and is not included in his income for 2024. The next \$10,000 of the distribution is not includable in 2024 income because it was included previously (conversion contribution). The remaining \$2,000 represents earnings on the contributions and is taxable and subject to the 10% early withdrawal penalty.

**Five-year rule.** The 5-year holding period begins on the first day of the tax year for which the taxpayer first contributed or converted money into a Roth IRA and ends on the last day of the fifth consecutive year. This is a once-in-a-lifetime qualification rule. Once a taxpayer has met the 5-year holding period for the first contributory Roth IRA, all subsequent contributory Roth IRAs are treated as having met the 5-year holding period.

**Note:** One 5-year holding period applies to all contributions made to any Roth IRA the taxpayer has. However, a separate 5-year period applies to each conversion from a traditional IRA to a Roth IRA as well as amounts rolled over from a qualified retirement plan to a Roth IRA. See *10% early withdrawal penalty*, below.

## Distributions After Roth IRA Participant's Death

The required minimum distribution (RMD) rules do not apply while the participant is alive. At the death of the Roth IRA participant, the RMD rules apply to the beneficiary as though the Roth IRA owner was subject to RMD rules and died before his or her required beginning date. See *Inherited IRA*, page 13-22.

Distributions from an inherited Roth IRA are tax free unless the Roth IRA participant did not meet the 5-year holding period requirement for contributions or conversions.

## Conversion Rules

There are no modified AGI limits or filing status requirements relating to rollovers from eligible retirement plans into Roth IRAs.

**Conversion contribution.** Money distributed from a qualified plan or IRA and reinvested within 60 days into a Roth IRA is called a conversion contribution. The distribution is taxable to the extent it does not represent a return of nondeductible basis. A conversion contribution is not subject to the 10% early withdrawal penalty. A conversion contribution can also be accomplished through a trustee-to-trustee transfer or a same trustee transfer where the trustee simply redesignates a traditional IRA as a Roth IRA rather than open up a new account or issue a new contract.

**Employer plan conversions.** Money in an employer-sponsored retirement plan, such as a 401(k), annuity, 403(b), government-deferred compensation (§457 plan), or profit-sharing plan, may be directly converted to a Roth IRA, subject to the same rules and limitations that apply to IRA to Roth IRA conversions. (Notice 2009-75)

**In-plan Roth rollovers.** A 401(k) plan can permit a participant to rollover an amount from his or her regular (pre-tax) elective deferral account into a designated Roth account in the same plan, regardless of whether the participant is eligible for a distribution from the regular account. [IRC §402A(c)(4)(E)]

**Income.** Include in income in the year of conversion the amount of the distribution from an eligible retirement account that would have been included in gross income if the taxpayer had not converted it to a Roth IRA.

**Required minimum distribution (RMD).** An amount distributed from a traditional IRA to meet RMD rules does not qualify for conversion into a Roth IRA.

**Inherited IRA.** An inherited traditional IRA from someone other than a spouse cannot be converted into a Roth IRA.

**Fair market value (FMV).** The tax paid on conversion is based on the FMV of the IRA or employer plan immediately prior to the conversion. FMV for purposes of an annuity contract that is converted soon after it is purchased must be computed using the premiums paid for the contract, not the cash surrender value.

**Author's Comment: Backdoor Roth.** If a taxpayer above the phase-out amounts wants to contribute to a Roth IRA he or she can make a nondeductible contribution to a traditional IRA and then immediately convert it to a Roth IRA (backdoor Roth). Due to the distribution rules for traditional IRAs, this works best if the taxpayer has no other traditional, SEP, or SIMPLE IRAs. See *IRA Distributions*, page 13-8

**10% early withdrawal penalty.** The 10% early withdrawal penalty will not apply to any distribution from a conversion contribution that has met the 5-year holding period requirement. For this purpose, the 5-year holding period applies separately to each conversion contribution and is not necessarily the same as the 5-year holding period used for determining the tax-free distribution rules. [Reg. §1.408A-6, *Answer A-5(c)*]

**Example:** Mary, a calendar year taxpayer, makes a conversion contribution on February 25, 2024, and makes a regular contribution for 2023 on the same date. The 5-year period for the conversion begins January 1, 2024, while the 5-year period for the regular contribution begins on January 1, 2023.

If the 5-year holding period is not met on a conversion contribution, the 10% penalty applies unless the distribution meets one of the other exceptions to the 10% early withdrawal penalty rules. See *Exceptions to the 10% Penalty on Early Distributions*, page 13-3.

## Recharacterization

**Recharacterization of a contribution to an IRA.** A recharacterization allows a taxpayer to treat a regular contribution made to a Roth or to a traditional IRA as having been made to the other type of IRA. A recharacterization does not include a conversion or any other rollover.

**Recharacterization of a regular IRA contribution.** To recharacterize a regular IRA contribution, a taxpayer tells the trustee of the financial institution holding his or her IRA to transfer the amount of the contribution plus earnings to a different type of IRA (either a Roth or traditional) in a trustee-to-trustee transfer or to a different type of IRA with the same trustee. If the recharacterization is done by the due date for filing his or her tax return (including extensions), the taxpayer can treat the contribution as made to the second IRA for that year.

**Rollovers or conversion to a Roth IRA.** A conversion from a traditional IRA, SEP IRA, or SIMPLE IRA to a Roth IRA cannot be recharacterized. In addition, amounts rolled over to a Roth IRA from other retirement plans, such as 401(k) or 403(b) plans, cannot be recharacterized.

**Decedent.** An election to recharacterize can be made on behalf of a decedent by the executor, administrator, or other person responsible for filing the decedent's final tax return.

## Roth IRA Reporting

Roth IRAs are reported on the tax return as follows.

- Contributions are not deductible and are not reported anywhere on a taxpayer's return.
- Conversions are either partially or fully taxable and are reported in Part II, Form 8606, *Nondeductible IRAs*.
- Taxable distributions and distributions meeting the qualified first-time homebuyer exception are reported in Part III, Form 8606.
- Nontaxable distributions (other than first-time homebuyer distributions) are reported on line 4a, Form 1040, with zero flowing to line 4b, Form 1040.
- If a contribution was made to a traditional IRA, and the taxpayer later recharacterized a part as a Roth IRA, report the nondeductible traditional IRA portion of the remaining contribution on Part I, Form 8606. If all of the contribution is recharacterized as a Roth IRA, do not report any amount on Form 8606. Attach a statement to the return explaining the recharacterization.
- If a contribution was made to a Roth IRA and later recharacterized all or a part as a traditional IRA, report the nondeductible traditional IRA portion on Part I, Form 8606. Do not report any remaining Roth IRA portion of the contribution on Form 8606. Attach a statement to the return explaining the recharacterization.

## Roth 401(k) and Roth 403(b) Plans

Taxpayers can make 401(k) type elective deferral contributions into Roth retirement accounts (IRC §402A). Rather than using pre-tax earnings, the Roth 401(k) elective deferral contributions are made with after-tax earnings. Qualified Roth 401(k) distributions receive the same tax-free treatment as qualified distributions from Roth

IRAs. Most of the other rules for the Roth 401(k) and Roth 403(b) accounts are the same as traditional 401(k) and 403(b) plans.

### Differences between a Roth IRA and a Roth 401(k):

- Contributions are limited by the elective deferral limits of 401(k) plans (\$23,000 for 2024 for a participant under age 50).
- Participants in Roth 401(k) plans are not subject to the modified AGI phaseout rules that apply to Roth IRAs. That means taxpayers with AGI above \$240,000 (2024 phaseout for MFJ) can still make Roth 401(k) contributions. However, they are subject to the highly-compensated employee rules which limit their contribution to the actual deferral percentage of other employees.
- If the plan allows, the employee has the option of receiving employer matching contributions as Roth contributions. These employer contributions are not excludable from gross income and are reported to the taxpayer in boxes 1 and 2a, Form 1099-R with code G in box 7.
- Ordering rules for Roth IRA distributions (see *Distributions*, page 13-12) do not apply to Roth 401(k) nonqualified distributions. Taxable earnings must be allocated to the distributions. (Reg. §1.402A-1)

**Example:** Jim took a \$5,000 nonqualified distribution from his Roth 401(k). The account contained \$9,000 of contributions and \$1,000 of earnings. Gross income must include allocated earnings of \$500 ( $\$1,000 \div \$10,000 \times \$5,000$ ). The 10% penalty may also apply.

**New for 2024** **Required minimum distribution (RMD).** RMD rules do not apply before the death of a participant in a designated Roth account in an employer plan. [IRC §402A(d)(5)]

## Simplified Employee Pension (SEP)

### Cross References

- Form 5305-SEP, *Simplified Employee Pension—Individual Retirement Accounts Contribution Agreement*
- IRS Pub. 560, *Retirement Plans for Small Business (SEP, SIMPLE, and Qualified Plans)*
- IRC §408(k), *Simplified employee pension defined*

### Related Topics

- Retirement Savings Contributions Credit, page 11-16
- Small Business Retirement, Tab 29
- Credit for Small Employer Pension Plan Startup Costs, Auto-Enrollment, and Military Spouse Participation (Form 8881), page 31-10

### SEP IRAs

A SEP is a written plan that allows the employer to make deductible contributions into an individual retirement arrangement (IRA) on behalf of the employee (SEP IRA). For this purpose, a self-employed individual can contribute to his or her own SEP. The SEP IRA is owned and controlled by each employee (or self-employed individual). The employer makes contributions to the financial institution where the employee maintains his or her SEP. As an IRA, the employee is always fully vested in the account and has complete freedom to move the funds or withdraw the funds at any time.

**Eligible employees.** The employer cannot discriminate against any employee that meets all the following.

- Has reached age 21,
- Has worked for the employer in at least three of the immediately preceding five years, and
- Has received at least \$750 in compensation from the employer during 2024.

**Contributions.** The employer, and not the employee, makes deductible contributions to the employee's SEP IRA. The employer must contribute the same percentage of compensation to the accounts for all eligible employees. If the employer is self-employed and contributes to his or her own SEP, the same percentage has to be contributed to the accounts of all eligible employees of the self-employed individual.

See *Pension Plan Limitations*, page 13-2, for contribution limits.

The employer cannot withhold the contribution from the employee's Form W-2 wages.

**Exception:** SARSEPs established by employers prior to 1997 can allow for employee elective deferral contributions under similar rules that apply to 401(k) plans.

**Roth contributions.** SEP plans (excluding SARSEPs) can allow employees to treat employee and employer SEP contributions as Roth contributions (in whole or in part). A plan which is designated as a Roth IRA cannot be treated as a SEP unless the employee elects that treatment.

Employer contributions made to a Roth SEP IRA must be reported to the employee for the year in which the contributions are made. These contributions are not excludable from gross income and are reported in boxes 1 and 2a, Form 1099-R with either code 2 or 7 in box 7 and the IRA/SEP/SIMPLE checkbox checked.

**Where to deduct SEP IRA contributions:**

- **Sole proprietors.** Deduct contributions made on behalf of employees on the pension and profit-sharing plans deduction line of Schedule C (Form 1040) or Schedule F (Form 1040). Deduct non-Roth contributions made on behalf of the sole proprietor on line 16, Schedule 1 (Form 1040), *Additional Income and Adjustments to Income*.
- **Partnerships.** Deduct contributions made on behalf of employees on line 18, Form 1065. The partnership must make the contribution on behalf of the partners and report the amount on line 13 (code R) of the partner's Schedule K-1 (Form 1065).

**Planning Tip:** If income limitations allow, a sole proprietor may want to contribute to a traditional IRA before contributing to his or her SEP IRA because contributions to a SEP IRA reduce the taxpayer's qualified business income (QBI) to compute the QBI deduction, whereas contributions to a traditional IRA do not

**Annual contributions.** The employer does not have to make contributions every year, nor do the compensation percentages have to be the same each year, as long as all eligible employees receive the same percentage of compensation treatment for a particular year. This is true even for employees who die or terminate employment before the contributions are made.

**More than one plan.** The allowed annual contribution to a SEP IRA is limited to the lesser of \$69,000 (for 2024), or 25% of the participant's compensation (20% of net self-employment income after one-half SE tax deduction). When computing this limit, add all contributions to all defined contribution plans maintained by the same employer (and any related employer).

**Example #1:** Greg, age 46, is employed by an employer with a 401(k) plan and he also works as an independent contractor for an unrelated business. Greg sets up a SEP IRA plan for his independent contracting business. Greg contributes the \$23,000 maximum amount to his employer's 401(k) plan for 2024. Greg would also like to contribute the maximum amount to his SEP IRA plan. He has enough earned income from his business to contribute the maximum for the year, \$69,000 to his SEP IRA plan. This limit is not reduced by the elective deferrals under his employer's plan because the limit on annual additions applies to each plan separately.

**Example #2:** Assume the same facts as Example #1, except Greg is 100% shareholder in the corporation in which he is employed. Even

though he has enough earned income from his independent contractor business to contribute the maximum of \$69,000, because the 401(k) plan and the SEP IRA plan are maintained by the same or related employer, the maximum Greg may contribute to his SEP IRA is \$46,000 (\$69,000 – \$23,000).

**Self-employed deduction limit.** Self-employed individuals must make a special computation to determine the maximum deduction for making SEP IRA contributions. Net earnings from self-employment must be reduced by one-half of SE tax and the SEP IRA contribution before applying the contribution rate. The following chart, converts the contribution rate for employees to the rate for self-employed individuals.

**Self-Employed SEP IRA Contribution Rates**

Contribution rate for employees	Rate applied to net SE income minus one-half SE tax	Rate applied to net SE income before deducting one-half SE tax*
1%	0.9901%	0.9202%
2%	1.9608%	1.8223%
3%	2.9126%	2.7068%
4%	3.8462%	3.5745%
5%	4.7619%	4.4255%
6%	5.6604%	5.2605%
7%	6.5421%	6.0799%
8%	7.4074%	6.8841%
9%	8.2569%	7.6736%
10%	9.0909%	8.4486%
11%	9.9099%	9.2098%
12%	10.7143%	9.9574%
13%	11.5044%	10.6916%
14%	12.2807%	11.4131%
15%	13.0435%	12.1220%
16%	13.7931%	12.8186%
17%	14.5299%	13.5034%
18%	15.2542%	14.1765%
19%	15.9664%	14.8384%
20%	16.6667%	15.4892%
21%	17.3554%	16.1293%
22%	18.0328%	16.7588%
23%	18.6992%	17.3781%
24%	19.3548%	17.9874%
25%	20.0000%	18.5870%

\* Assumes participant has not exceeded the maximum earnings subject to Social Security tax.

**Example:** Larry is a self-employed carpet cleaner with one employee. He contributes to a SEP IRA plan for himself and his employee. Larry's Schedule C (Form 1040) net income equals \$40,000 and his deduction for one-half SE tax equals \$2,826. Assume Larry contributes 15% of his employee's Form W-2 wages to a SEP IRA. Larry's self-employment SEP IRA contribution for himself can be calculated three different ways.

$$\$40,000 \times 12.1220\% = \$4,849,$$

$$\$40,000 - \$2,826 = \$37,174 \times 13.0435\% = \$4,849, \text{ or}$$

$$\$40,000 - \$2,826 = \$37,174 - \$4,849 = \$32,325 \times 15\% = \$4,849.$$

**Note:** Using the 12.1220% only works if Larry does not exceed the Social Security maximum earnings for the year. If earnings exceed the maximum, the middle column calculation method must be used.

**Savings Incentive Match Plans for Employees (SIMPLE)**

**Cross References**

- IRS Pub. 560, *Retirement Plans for Small Business (SEP, SIMPLE, and Qualified Plans)*
- IRC §408(p), *Simple retirement accounts*
- IRS Notice 98-4

## Related Topics

- Retirement Savings Contributions Credit, page 11-16
- SIMPLE 401(k) Plan, page 29-18
- Credit for Small Employer Pension Plan Startup Costs, Auto-Enrollment, and Military Spouse Participation (Form 8881), page 31-10

## SIMPLE IRAs

A SIMPLE IRA allows employees to choose the financial institution that will serve as trustee. The employee also has the right to roll over or transfer funds in a SIMPLE IRA to another financial institution at any time without having to first meet any vesting requirements. As an IRA, the SIMPLE plan does not have vesting rules. Participants are always 100% vested in the plan, including employer matching contributions.

**Eligible employers.** Employers can set up a SIMPLE IRA for employees if they have 100 or fewer employees who received \$5,000 or more in compensation from the employer in the preceding year. The employer cannot maintain another qualified plan (except for certain union employees). The 100-employee limit must be met each year to continue contributing to the plan. A two-year grace period applies once this limit is exceeded.

**Eligible employees.** Any employee who received at least \$5,000 in compensation from the employer during any two years prior to the current year, and reasonably expects to receive at least \$5,000 in compensation during the current year, is eligible to participate in the employer's SIMPLE plan. The employer can offer the plan on a less restrictive basis but cannot make the plan participation rules any more restrictive.

**Self-employed individual.** A self-employed individual is treated as both an employee and the employer of his or her business. Compensation equals net earnings from self-employment before subtracting any contributions made to the SIMPLE IRA.

**Deadline for setting up a SIMPLE IRA.** A SIMPLE IRA plan can be set up effective on any date from January 1 through October 1 of a year, provided the employer did not previously maintain a SIMPLE IRA plan. A SIMPLE IRA must be set up for an employee before the first date a contribution is required to be deposited into the employee's IRA. If the employer is a new employer that came into existence after October 1, the plan can be set up as soon as administratively feasible after the business comes into existence. A SIMPLE plan cannot have an effective date that is before the date the plan is actually adopted.

**Deadline for making contributions.** Employers must contribute employee elective deferral (salary reduction) amounts to the SIMPLE IRA of an employee within 30 days after the end of the month in which the amounts would otherwise have been payable to the employee in cash. Employer matching contributions are due by the due date, including extensions, for filing the tax return.

**Self-employed.** A self-employed taxpayer must deposit salary reduction contributions within 30 days after the end of the tax year. For calendar year taxpayers, this means salary reduction contributions for 2024 must be made by January 30, 2025. Employer contributions must be deposited by the due date, including extensions, for filing the tax return.

## SIMPLE IRA Contributions

Contributions to SIMPLE IRAs are made up of two parts.

- Employee elective deferrals (limited to \$16,000, \$19,500 age 50 and over).
- Employer matching contributions.

**New for 2024** **Increased employee elective deferral limit.** The employee elective deferral limit is increased by 110% (\$17,600,

\$21,450 age 50 and over) if the employer has no more than 25 employees (who have at least \$5,000 in compensation for the year), or a large employer with more than 25 employees elects to have the higher 110% limit apply.

**Employee elective deferrals.** During the 60-day period before the beginning of any year, and during the 60-day period before the employee is eligible, the employee can choose the amount to defer from wages into the SIMPLE IRA, expressed either as a percentage of compensation or a specific dollar amount. The election to defer wages can be cancelled at any time during the year. For information on excess deferrals, see *Excess deferrals*, page 29-17.

**Employer contributions.** An employer can choose to either match the elective deferrals of employees or make nonelective contributions on behalf of all eligible employees. Employer matching contributions are typically dollar-for-dollar of the employee's elective deferral up to 3% of the employee's compensation for the year. Nonelective contributions must equal 2% of employee compensation for all employees, including those who choose not to make elective deferral contributions. See *SIMPLE IRA Plan*, page 29-9.

**Roth contributions.** SIMPLE IRA plans can accept Roth contributions. A plan which is designated as a Roth IRA cannot be treated as a SIMPLE IRA plan unless the employee elects that treatment.

Employer contributions made to a Roth SIMPLE IRA must be reported to the employee for the year in which the contributions are made. These contributions are not excludable from gross income and are reported in boxes 1 and 2a, Form 1099-R with either code 2 or 7 in box 7 and the IRA/SEP/SIMPLE checkbox checked.

**Employees who participate in other plans.** If an employee participates in another employer's qualified plan that allows for elective deferrals [such as a 401(k) plan], the total combined elective deferrals for both plans cannot exceed the annual limit for 401(k) plans (\$23,000 in 2024 for employees under age 50). The employee is responsible for monitoring compliance in this situation.

### Where to deduct SIMPLE IRA contributions:

- **Employers.** The employer deducts contributions on behalf of employees as a business deduction. For example, a sole proprietor deducts the contributions on behalf of common-law employees on Schedule C (Form 1040) or Schedule F (Form 1040), and excludes non-Roth contributions from Form W-2 wages. However, the employee's elective deferrals are subject to FICA and should be included in Social Security and Medicare wages on Form W-2 (also subject to FUTA).
- **Self-employed.** A self-employed taxpayer deducts non-Roth elective deferrals and employer matching contributions on line 16, Schedule 1 (Form 1040), *Additional Income and Adjustments to Income*.

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**Example:** Tony's share of profits on his Schedule K-1 from the Gopher Partnership is \$90,000. Tony elects to defer \$10,000 to his SIMPLE IRA. Compensation for purposes of the employer's match is \$83,115 (net self-employment). Assume Gopher Partnership makes 2% nonelective contributions for all partners and employees of Gopher. The employer's 2% contribution for Tony is \$1,662 (\$83,115 × 2%). Tony's Schedule K-1 shows \$11,662 on line 13, code R, and he deducts that amount on line 16, Schedule 1 (Form 1040), *Additional Income and Adjustments to Income*.

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## SIMPLE IRA Distributions

Distributions are generally treated the same as distributions from any other IRA, with the exception of the 2-year rule.

**2-year rule.** Funds in a SIMPLE IRA must remain in a SIMPLE IRA for at least two years from the date the employee first participated in the employer's SIMPLE plan before they can be rolled

over into any other type of retirement plan (including traditional IRAs). However, rollovers are permitted from one SIMPLE IRA to another SIMPLE IRA during the 2-year period. The 2-year period begins on the first day on which contributions made by the employer are deposited into the employee's SIMPLE IRA.

**25% early withdrawal penalty.** The 10% early withdrawal penalty that applies to other retirement plans and IRAs also applies to SIMPLE IRAs. However, the 10% penalty is increased to 25% if the early withdrawal occurs during the initial 2-year period.

## Other Retirement Plans

### Cross References

- IRS Pub. 560, *Retirement Plans for Small Business (SEP, SIMPLE, and Qualified Plans)*
- IRS Pub. 571, *Tax-Sheltered Annuity Plans (403(b) Plans)*
- IRS Pub. 575, *Pension and Annuity Income*
- IRS Pub. 721, *Tax Guide to U.S. Civil Service Retirement Benefits*
- IRS Pub. 939, *General Rule for Pensions and Annuities*
- IRC §401, *Qualified pension, profit-sharing, and stock bonus plans*
- IRC §4975(e)(7), *Employee stock ownership plan*

### Related Topics

- Small Business Retirement Plans, Tab 29
- Credit for Small Employer Pension Plan Startup Costs, Auto-Enrollment, and Military Spouse Participation (Form 8881), page 31-10

### Qualified Plans

A qualified retirement plan must be for the exclusive benefit of employees or their beneficiaries. Employer contributions are generally tax deductible on the employer's tax return and excluded from the employee's wages. Contributions and earnings are generally tax free until distributed. See *Qualified Plans*, page 29-11.

**Contribution and deduction limits.** Taxpayers may have more than one qualified plan, but the contributions to all the plans must not total more than the overall annual limits. The deduction limit depends on the type of plan being funded. See *Pension Plan Limitations*, page 13-2.

**Compensation limit.** For purposes of calculating deductible employer contributions to a qualified plan, the maximum compensation that can be taken into account is limited. For compensation limits, see *Pension Plan Limitations*, page 13-2.

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**Example:** Mushi Incorporated has a profit-sharing plan that contributes 10% of wages to the accounts of eligible employees. Elizabeth is an executive with a salary of \$350,000 in 2024. Mushi Incorporated's deduction for the contribution to Elizabeth's account is limited to \$34,500 ( $\$345,000 \times 10\%$ ).

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**Example:** Bianca Incorporated has a defined benefit plan that provides employees a pension benefit of 2% of compensation multiplied by the number of years of service. Kataan is an executive with a salary of \$400,000 and 17 years of service. Kataan will receive an annual pension of \$117,300 ( $\$345,000 \times 2\% \times 17$  years).

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**Nondeductible employee contributions.** Qualified plans can allow for employees to make nondeductible contributions to the plan. Even though they are not deductible, the earnings on them are tax free until distributed.

**Automatic enrollment.** To encourage employees to save for retirement, an employer may add automatic enrollment to any plan that allows elective deferrals. The employer must give employees notice of the amount withheld and allow employees to change or stop the withdrawal. The plan may also give employees the option to withdraw contributions within 90 days of the first contribution.

**Multiple businesses.** If the taxpayer has more than one business, but only one has a retirement plan, only the earned income from that business is considered for that plan. [Reg. §1.401-10(b)(2)]

**Reporting requirements.** The administrator or sponsor of a qualified plan is required to file either Form 5500, *Annual Return/Report of Employee Benefit Plan*, Form 5500-SF, *Short Form Annual Return/Report of Small Employee Benefit Plan*, or Form 5500-EZ, *Annual Return of A One-Participant (Owners/Partners and Their Spouses) Retirement Plan or A Foreign Plan*, on an annual basis.

### Defined Contribution Plans

A defined contribution plan is a qualified plan that provides an individual account for each participant in the plan. Benefits depend upon the amount contributed, income, expenses, gains, losses, and forfeitures of other accounts that may be allocated to a participant's account. Examples of defined contribution plans include profit-sharing plans, 401(k) plans, 403(b) plans, and money purchase plans.

### Defined Benefit Plans

A defined benefit plan is any qualified plan that is not a defined contribution plan. Contributions are based on what is needed to provide definitely determinable benefits to plan participants. Actuarial assumptions and computations are required to determine these contributions. Forfeitures under a defined benefit plan cannot be used to increase the benefits any employee would otherwise receive under the plan. Instead, they are used to reduce employer contributions.

### Section 401(k) Plans

A 401(k) plan is a qualified defined contribution plan that can include a cash or deferred arrangement under which participants can choose to have part of their before-tax compensation contributed to the plan rather than receive the compensation in cash. The employee contributions are called elective deferrals. Employers can, but are not required to, make matching contributions. For elective deferral limits, see *Pension Plan Limitations*, page 13-2.

**Time limit for employers to contribute elective deferrals.** When employers withhold elective deferrals from the wages of employees, the employer is required to deposit the funds into the employee's account as soon as it is reasonably possible to do so, but no later than the 15th business day of the month following the payday.

**Excess contributions of highly-compensated employees.** The law has complex tests to prevent discrimination in a 401(k) plan. Such tests as the actual deferral percentage (ADP) test and the actual contribution percentage (ACP) test are designed to limit plan benefits for highly-compensated employees. These rules are avoided when plans are set up as SIMPLE 401(k) or safe harbor 401(k) plans.

**SIMPLE 401(k) plan.** Employers with 100 or fewer employees who earned \$5,000 or more during the preceding year may be able to set up a SIMPLE 401(k) plan.

**Safe harbor 401(k) plans.** A safe harbor 401(k) plan is similar to a traditional 401(k) plan but must provide for employer matching contributions that are fully vested. By meeting these requirements, the 401(k) avoids the complex nondiscrimination testing rules. Safe harbor 401(k) plans are also well suited for self-employed individuals.



**Example:** Tammy is under age 50 and is a self-employed author. She wants to put away as much as possible in a qualified retirement plan. She sets up a single-participant safe harbor 401(k) plan. For 2024, her net profit after the one-half SE tax deduction is \$30,000. She contributes the maximum elective deferral of \$23,000 to the plan. The plan is also set up to contribute the maximum employer deduction, which is 25% for employees, or 20% for self-employed individuals. Since elective deferrals do not reduce compensation for purposes of the deduction limit, her employer matching contribution is \$6,000 ( $\$30,000 \times 20\%$ ). The total of employer contributions (\$6,000) plus elective deferrals (\$23,000) equals \$29,000, which is 97% of her total SE earnings.

For more information on SIMPLE 401(k), safe harbor 401(k), and solo 401(k) plans, see *Small Business Retirement*, Tab 29.

## Section 403(b) Tax-Sheltered Annuity Plans

Section 403(b) annuity plans generally allow for the same elective deferral arrangements as section 401(k) plans. However, the types of employees eligible to participate are generally limited to employees of tax-exempt organizations, public schools, civilian faculty and staff of the Uniformed Services University of the Health Sciences, and certain ministers.

**403(b) elective deferral limits.** Limits are generally the same as section 401(k) plan limits. See *Pension Plan Limitations*, page 13-2.

## Employee Stock Ownership Plan (ESOP)

An ESOP is a qualified stock bonus plan or a combination stock bonus and money purchase plan. ESOPs are designed to invest primarily in employer securities.

**Distributions.** Distributions from ESOPs are taxed like distributions from other qualified plans. The amount included is the FMV of the distribution minus the amount of employee after-tax contributions. However, since distributions from ESOPs often are made in the form of employer securities, the rules on net unrealized appreciation may apply.

**Net unrealized appreciation.** Net unrealized appreciation (NUA) is the increase in value of employer securities while in the qualified plan. If the distribution is a lump-sum distribution, the NUA is taxed only when the securities are sold unless the taxpayer makes an election to include it in income in the year received. The election is made on Form 4972, *Tax on Lump-Sum Distributions*.

**Example:** Total employer securities purchased for Amanda's ESOP over the years equal \$20,000. Amanda leaves her job when these employer securities are worth \$70,000. The securities, rather than cash, are distributed to Amanda, who pays tax at her ordinary rate on the \$20,000 distribution, which becomes her cost basis in the securities. She waits until they are worth \$100,000 before selling them. The \$80,000 gain (\$100,000 minus \$20,000) is taxed at her long-term capital gain rate rather than her ordinary income rate.

## Section 457 Deferred Compensation Plans

Generally, section 457 plans are offered only to employees of state or local governments and tax-exempt organizations. Participants in eligible section 457 plans are not taxed currently on pay that is deferred under the plan or on any earnings from the plan's investment of the deferred pay. Participants in eligible state or local government plans are taxed when amounts are distributed. Participants in eligible tax-exempt organizations are taxed when amounts are distributed or otherwise made available to the participant. For more information, see *Section 457 Deferred Compensation Plans*, page 29-23.

## Vesting Rules

A qualified retirement plan must meet certain vesting rules. A vested benefit means an employee's right to the benefit is non-forfeitable upon the attainment of normal retirement age.

**Employee contributions.** An employee must always be fully vested in his or her own contributions to the plan, such as employee elective deferrals to a 401(k) plan.

**Employer contributions.** An employee must become vested in employer contributions under the following schedule.

- 1) The employee becomes fully vested after completing at least three years of service (five years for defined benefit plans), or
- 2) The employee is partially to fully vested under the following schedule.

Years of Service	Percent of Vested Benefits	
	Defined Contribution Plans	Defined Benefit Plans
2.....	20%	
3.....	40%	20%
4.....	60%	40%
5.....	80%	60%
6 or more.....	100%	80%
7 or more.....		100%

**Note:** Employers can choose to allow employees to be vested sooner than the above schedules. [IRC §411(a)(2)]

**Author's Comment:** A participant in an employer qualified plan is generally limited in his or her ability to cash in funds, even if the employee is fully vested. Employees generally cannot cash in or roll over vested benefits into an IRA until the employee separates from service. In contrast, a participant is always fully vested in an IRA, SIMPLE IRA, SEP IRA, and a Roth IRA and does not need to first retire or separate from service to have access to funds in these accounts. Tax and the early withdrawal penalty may apply, but the employer cannot prevent the employee from cashing in one of these accounts.

## Deemed IRA

A qualified plan can maintain a separate account under the plan to receive voluntary employee contributions. This is called a Deemed IRA. If the separate account otherwise meets the requirements of an IRA, it is subject only to IRA rules. An employee's account can be set up as either a traditional IRA or a Roth IRA.

## Railroad Retirement

Benefits paid to retirees under the Railroad Retirement Act fall into two tiers.

- **Tier 1.** Tier 1 benefits are the equivalent of Social Security benefits that a railroad employee or beneficiary would have been entitled to receive under the Social Security system. For tax purposes, they are taxed the same as Social Security benefits.
- **Tier 2.** Tier 2 benefits are treated the same as if received from a qualified employee plan. They include employee after-tax contributions, as well as fully taxable vested dual benefits and supplemental annuity benefits. To determine the taxable and nontaxable portion of Tier 2 benefits, see *Distributions*, page 13-18.

**Employee contributions.** Railroad employees are covered under the Railroad Retirement Tax Act (IRC §3233). To the extent that railroad employees pay employment taxes at a rate greater than the rate paid by employees covered under Social Security, the excess employment taxes withheld are considered the employee's cost, or investment in railroad retirement benefits. The total amount of employee contributions is included in box 3, Form RRB-1099-R, *Annuities or Pensions by the Railroad Retirement Board*. This amount is not reduced by any amounts the RRB calculated as previously recovered. Box 3 is the latest amount reported and may have increased

or decreased from a previous Form RRB-1099-R. If this amount has changed, the tax-free part of Tier 2 benefits may need to be recalculated. If box 3 is blank, the full amount of Tier 2 benefits is taxable.

## Federal Retirement

**Federal Phased Retirement Program.** Federal employees otherwise eligible for retirement benefits can continue working on a reduced schedule and collect a corresponding percentage of their retirement benefits. The 10% early withdrawal penalty does not apply to distributions received by an employee participating in this program. [IRC §72(t)(2)(A)(viii)]

**Thrift Savings Plans.** The Thrift Savings Plan (TSP) is a retirement savings and investment plan for federal employees and members of the uniformed services including the Ready Reserve or National Guard. It was established by Congress in the Federal Employees' Retirement Act of 1986. The TSP is a defined contribution plan and offers the same types of savings and tax benefits that many private corporations offer their employees under 401(k) plans and contains a Roth option. For 2024, the contribution limit is \$23,000 (plus \$7,500 catch-up contribution limit if age 50 or older).

## Distributions

**Cost basis in a retirement plan.** Some retirement plans allow for after-tax contributions to the plan. When distributions from a pension or annuity plan include money that represents after-tax contributions, it is a recovery of the cost basis in the plan. The cost basis portion of each distribution is not taxable.

**Starting date before July 2, 1986.** If the annuity starting date was before July 2, 1986 and the 3-year rule was not used, use the general rule, below. If the 3-year rule was used, the annuity payments are generally now fully taxable.

**General rule method.** The general rule must be used to determine the tax-free portion of a distribution from a nonqualified plan, commercial annuity, and a qualified plan that cannot or does not choose to use the simplified method. Under the general rule, the amount of each payment that is more than the part that represents the net cost is taxable. The part that represents net cost equals the same proportion that the investment in the contract is to the expected return.

**Example:** Ralph, age 65, purchases an annuity for \$10,800 that will pay \$100 a month for life. According to Table V, *Ordinary Life Annuities, One Life—Expected Return Multiples*, in IRS Pub. 939, Ralph is expected to live 20 more years. Therefore, his expected return at the annuity start date is \$24,000 ( $\$100 \times 12 \times 20$ ). Ralph's cost divided by expected return equals 45% ( $\$10,800 \div \$24,000$ ). Each year until his total cost is recovered, the tax-free portion of his distributions is \$540 ( $\$1,200 \times 45\%$ ).

**Simplified method.** For qualified plans with a start date after July 1, 1986 and before November 19, 1996, the taxpayer could have chosen to use either the simplified method or the general rule. For qualified plans with annuity start dates after November 18, 1996, the simplified method must be used if one of the following is true.

- Participant is under age 75 on the annuity start date, or
- The participant is entitled to less than five years of guaranteed payments.

Nonqualified plans cannot use the simplified method.

Under the simplified method, the tax-free part of each annuity payment is calculated by dividing the cost basis by the total number of anticipated monthly payments. For an annuity that is payable over the lives of the annuitants, this number is based on the annuitants' ages on the annuity starting date and is determined from a table. For any other annuity, this number is the number of monthly annuity payments under the contract.

## Simplified Method Worksheet

- 1) Enter total pension or annuity payments received during the year. 1) \_\_\_\_\_
- 2) Enter cost basis in plan as of the start date..... 2) \_\_\_\_\_
- 3) Enter appropriate number from table, below ..... 3) \_\_\_\_\_
- 4) Divide line 2 by line 3..... 4) \_\_\_\_\_
- 5) Multiply line 4 by the number of months for which this year's payments were made. If annuity start date was before 1987, enter this amount on line 8 and skip lines 6, 7, 10, and 11..... 5) \_\_\_\_\_
- 6) Enter total cost basis previously recovered tax free in years after 1986 (line 10 previous year worksheet) ..... 6) \_\_\_\_\_
- 7) Subtract line 6 from line 2..... 7) \_\_\_\_\_
- 8) Enter the smaller of line 5 or line 7 ..... 8) \_\_\_\_\_
- 9) Taxable amount this year. Subtract line 8 from line 1 (not less than zero)..... 9) \_\_\_\_\_
- 10) Add line 6 and line 8..... 10) \_\_\_\_\_
- 11) Balance of cost to be recovered. Subtract line 10 from line 2..... 11) \_\_\_\_\_

## Tables for Line 3

Age at annuity start date:	Start date before November 19, 1996	Start date after November 18, 1996
55 or under .....	300 .....	360 .....
56 – 60.....	260 .....	310 .....
61 – 65.....	240 .....	260 .....
66 – 70.....	170 .....	210 .....
71 or over .....	120 .....	160 .....

Combined ages of annuitant and beneficiary at start date:	Start date after December 31, 1997
110 or under .....	410 .....
111 – 120 .....	360 .....
121 – 130 .....	310 .....
131 – 140 .....	260 .....
141 or over .....	210 .....

**Note:** Use the combined ages table only if the start date is after December 31, 1997, and annuity payments are based on the life of the annuitant and a beneficiary. Otherwise use the other table.

**Nonperiodic payments.** These are payments that are not periodic (annuity payments) and are not corrective distributions. If a qualified plan has a cost basis, the nontaxable portion of a nonperiodic payment is determined as follows.

- Distribution on or after annuity start date, all of the nonperiodic payment is taxable. If subsequent annuity payments are reduced because of the nonperiodic payment, a portion of the nonperiodic distribution is nontaxable. For calculation, see IRS Pub. 575, *Pension and Annuity Income*.
- Lump-sum distribution of entire amount in plan, the amount that exceeds the remaining cost basis is taxable.
- Distribution before annuity start date, use this formula:  

$$\text{Distribution} \times (\text{cost basis} \div \text{account balance}) = \text{tax-free amount.}$$

**U.S. civil service retirement benefits—alternative annuity option.** Retirees receiving U.S. civil service retirement benefits generally follow the same rules for recovering the cost basis as mentioned above. Retirees with a life threatening illness may be eligible for the alternative annuity option. If this choice is made, the participant will receive a lump-sum payment equal to the participant's contributions to the plan and a reduced monthly annuity. Special rules apply to the calculation of the taxable and nontaxable portion of the lump-sum payment option. For details, see IRS Pub. 721, *Tax Guide to U.S. Civil Service Retirement Benefits*.

## Retirement Plan Loans

If a taxpayer borrows money from his or her retirement plan, the loan is generally treated as a nonperiodic distribution. See *Loans treated as distributions*, page 29-20.

**Exception to loans-as-distribution rule.** If allowed by the plan, the loan is not a distribution as long as it is used by the taxpayer to purchase his or her main home, or must be repaid within five years. The maximum amount of the loan cannot exceed the lesser of \$50,000 or half the present value (but not less than \$10,000) of the taxpayer's vested benefit under the plan.

**Loan offsets.** A qualified plan loan offset amount is the amount that is treated as distributed from a qualified retirement plan, a section 403(b) plan, or a governmental section 457(b) plan because of termination of the plan or the failure to meet repayment terms of the loan because of the employee's severance from employment. The period during which a qualified loan offset amount may be contributed to an eligible retirement plan as a rollover contribution ends on the due date (including extensions) for filing the federal income tax return for the year in which the offset amount is treated as distributed from the plan.

## Survivors and Beneficiaries

A death benefit paid to a survivor or beneficiary of pension or annuity income is included in gross income in the same way the plan participant would have reported it. Beneficiaries can generally exclude part of each annuity (or lump-sum, if applicable) payment as a tax-free recovery of the participant's investment in the contract. See *Distributions*, page 13-18. See also *Income in Respect of a Decedent (IRD)*, page 21-8.

## Nonqualified Plans

Nonqualified plans are generally those plans that do not meet certain requirements under the Internal Revenue Code. A nonqualified plan may be used to reward highly-compensated employees and key executives without having to meet nondiscrimination rules that apply to qualified plans. In order for an employee to receive tax-deferred treatment, a nonqualified plan must either be unfunded, or the employee must be at risk to lose the benefits [IRC §3121(v)(2)]. The employer generally cannot deduct contributions to a nonqualified plan until they are included in the employee's taxable compensation. [IRC §404(a)(5)]

See *Nonqualified Deferred Compensation Plans*, page 29-22.

**Nonqualified annuities.** Taxpayers may own non-retirement plan annuities which are bought directly from the issuer. Withdrawals from these nonqualified annuities are allocated first to earnings and then to basis. Unless an exception applies, earnings withdrawn before age 59½ are subject to the additional 10% tax. For exceptions, see *Exceptions to the 10% Penalty on Early Distributions*, page 13-3.

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**Example:** In 2012, Tom purchased a nonqualified annuity for \$50,000. In 2024, the annuity is worth \$90,000. Tom, age 63, takes a withdrawal of \$50,000. \$40,000 of the withdrawal is taxable as earnings and \$10,000 is a nontaxable return of basis.

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**Annuity payments.** Annuity payments are contractual payments from an annuity paid over a specified time. The taxable amount of annuity payments from a nonqualified annuity is determined using the general rule. See *General rule method*, page 13-18.

## Lump-Sum Distributions

If a plan participant was born before January 2, 1936, and takes a lump-sum distribution from a qualified retirement plan and does not roll any of the distribution over into another plan or IRA, the participant may be eligible to elect to pay tax at the special 10-year averaging rates or treat a portion of the distribution as a capital gain taxed at the 20% tax rate. See IRS Pub. 575, *Pension and Annuity Income*. For any other lump-sum distribution, see *Nonperiodic payments*, page 13-18.

## Cross References

- IRS Pub. 590-A, *Contributions to Individual Retirement Arrangements (IRAs)*
- IRS Pub. 590-B, *Distributions from Individual Retirement Arrangements (IRAs)*
- IRC §402(c), *Rules applicable to rollovers from exempt trusts*
- Rev. Proc. 2016-47

## Related Topics

- Rollovers and Transfers, page 29-21

## Tax-Free Rollovers and Transfers

Funds from one retirement account (including IRAs) can be moved tax free into another account by means of one of the following.

- Rollover.
- Trustee-to-trustee transfer.
- Transfer incident to a divorce.

**Roth IRAs.** Special rules apply when funds from a traditional IRA are moved into a Roth IRA. See *Conversion Rules*, page 13-12.

## Rollover

A rollover is a tax-free distribution from one retirement plan that is then contributed to another retirement plan. The contribution to the second retirement plan is called a rollover contribution.

**60-day rule.** A taxpayer has until the 60th day following a distribution to make a rollover contribution. Distributions that are not rolled over in 60 days are taxable in the year distributed, even if the 60-day period expires in the following year. Contributions made after the 60-day period are treated as regular contributions.

**Disaster-related relief.** For qualified disaster distributions, taxpayers have up to three years to repay the distribution back into an eligible retirement plan. During this 3-year period, the disaster distribution is treated as an eligible rollover distribution, and any repayment is treated as having transferred the amount to the eligible retirement plan in a direct trustee-to-trustee transfer with 60 days of the distribution. See *Qualified Disaster Recovery Distributions*, page 13-23.

**Withdrawal and redeposit.** An individual may withdraw funds from an IRA for personal use and this may be considered a rollover as long as the money is redeposited into the same IRA or another qualified IRA within 60 days. (Ltr. Rul. 9010007)

**Self-certification for missed rollover deadline.** A taxpayer may make a written certification to a plan administrator or an IRA trustee that he or she missed the 60-day rollover contribution deadline because of one or more of the following reasons.

- An error was committed by the financial institution receiving the contribution or making the distribution to which the contribution relates.
- The distribution, having been made in the form of a check, was misplaced and never cashed.
- The distribution was deposited into and remained in an account that the taxpayer mistakenly thought was an eligible retirement plan.
- The taxpayer's principal residence was severely damaged.
- A member of the taxpayer's family died.
- The taxpayer or a member of the taxpayer's family was seriously ill.
- The taxpayer was incarcerated.
- Restrictions were imposed by a foreign country.
- A postal error occurred.

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- The distribution was made on account of a levy under IRC section 6331 and the proceeds of the levy have been returned to the taxpayer.
- The party making the distribution to which the rollover relates delayed providing information that the receiving plan or IRA required to complete the rollover despite the taxpayer's reasonable efforts to obtain the information.
- The distribution was made to a state unclaimed property fund.

A plan administrator or an IRA trustee may rely on the certification in accepting and reporting receipt of the rollover contribution.

A model letter for making the certification is in the appendix of Revenue Procedure 2020-46. The letter is not submitted to the IRS, but a copy of the certification should be kept in the taxpayer's filed and be available if requested on audit. (Rev. Proc. 2020-46)

**Kinds of rollovers.** See *Rollover Chart*, page 13-2.

**Nondeductible IRAs.** If funds from a traditional IRA are rolled into a qualified retirement plan (not another traditional IRA), then the amount rolled over is considered to have come first from tax-deferred amounts before after-tax amounts.

**Example:** Char has a traditional IRA with a value of \$10,000 and a nondeductible basis of \$3,000. Char rolls \$7,000 into her new employer's qualified plan. The rollover consists of the tax-deferred amount, leaving the nondeductible basis of \$3,000, the remaining balance in her IRA.

**Nondeductible qualified plan contributions.** When nondeductible employee contributions are included in a rollover from an employer qualified plan into a traditional IRA or SEP IRA, the nondeductible portion should be added to the basis of the IRA on line 2, Form 8606, *Nondeductible IRAs*.

**One-year waiting period rule.** If any part of a distribution from a traditional IRA is rolled over tax free, no other rollover from that same IRA is allowed within a 1-year period. Likewise, a distribution from the IRA that accepted the tax-free rollover cannot be rolled over within the same 1-year period. The 1-year period begins on the date the IRA distribution is first received, not the date it was rolled over into an IRA. See *All IRAs aggregated*, below.

**All IRAs aggregated.** A taxpayer can make only one rollover from an IRA to another (or the same) IRA in any one-year period regardless of the number of IRAs owned. The limit applies by aggregating all of a taxpayer's IRAs, including SEP and SIMPLE IRAs as well as traditional and Roth IRAs, effectively treating them as one IRA for purposes of the one-year rule. However, trustee-to-trustee transfers between IRAs and rollovers from traditional IRAs to Roth IRAs (conversions) are not limited. See *Conversion Rules*, page 13-12. [IRC §408(d)(3)(B)]

**Example:** Justin has three traditional IRAs and on January 1, 2024, he took a distribution from IRA-1 and rolled it over into IRA-2 on the same day. For 2024, Justin cannot roll over any other 2024 IRA distribution, including a rollover distribution involving IRA-3.

**Same property rule.** If property is distributed from an IRA, the same property must be contributed to a new IRA to qualify for tax-free rollover treatment.

**Example:** Eric owns 200 shares of Oshkosh Truck inside his IRA. Eric can roll those specific 200 shares of stock over into a new IRA tax free. He cannot have the 200 shares of stock distributed and have substitute stock contributed to the new IRA and call it a tax-free rollover. The same shares distributed must be contributed to the new IRA to qualify for tax-free rollover treatment.

**Letter Ruling:** The taxpayer took a distribution from one IRA, purchased real estate with the funds, and then attempted to roll over the real estate into a second IRA. The IRS ruled that an individual cannot purchase real estate with the funds distributed from an IRA and roll over such purchased property into another IRA (Ltr. Rul. 200647028).

The taxpayer should have first found an IRA trustee willing to hold real estate inside the IRA, roll over the funds from the first IRA to this new IRA, and then have the new IRA purchase the real estate.

**Exception to the same property rule.** If property is distributed from a qualified retirement plan that is an eligible rollover distribution, the property can be sold, and the cash proceeds from the sale can be contributed to a traditional IRA in place of the property as a tax-free rollover. However, the taxpayer cannot keep the property distributed and substitute other cash for the property received. Tax-free rollover treatment only applies if the property itself is contributed to the new IRA, or the property is sold and the proceeds are rolled over into the new IRA.

**Partial rollover.** The amount rolled over into a new IRA or qualified plan does not have to be equal to the amount distributed from the old plan. The amount not rolled over is taxable, except for the part that is a return of nondeductible basis.

**Court Case:** A taxpayer made a \$120,000 withdrawal from his IRA on February 15 and another withdrawal of \$168,000 on April 9. The taxpayer made a rollover contribution of \$120,000 on April 30. The IRS originally disallowed the rollover as it had taken place greater than 60 days from the February 15 withdrawal. Upon appeal, the court allowed the rollover stating that it was a partial rollover of the \$168,000 withdrawal 21 days prior to the contribution. (*Haurly*, 8th Cir., May 12, 2014)

**Required minimum distribution.** Any amounts distributed to satisfy the RMD rules do not qualify for tax-free rollover treatment. See *Required Minimum Distribution (RMD)*, page 13-21.

**Inherited IRAs.** See *Inherited IRA*, page 13-22.

**How to report a rollover.** Enter the total distribution on line 4a of Form 1040. Enter any taxable amount not rolled over on line 4b. Write "Rollover" next to line 4b.

**20% withholding requirement.** Distributions from qualified employer plans are required to have 20% withheld for federal income tax. The withholding requirement applies even if the participant plans to roll over the distribution into a traditional IRA. Mandatory withholding can be avoided by choosing a direct rollover option. See *Direct rollovers*, page 13-21.

**Exceptions:** The payer does not have to withhold federal income tax if any of the following conditions apply.

- Total distributions during the year are less than \$200.
- Total distribution consists solely of employer securities, plus cash of \$200 or less in lieu of fractional shares.
- Distribution is from an IRA.
- Distribution is not eligible for tax-free rollover treatment.

• **Note:** Any amount withheld is part of the distribution. If the rollover amount is less than the total distribution, the difference is taxable to the extent the distribution does not represent after-tax basis.

**Example:** Kent changes jobs and wants to roll over the entire \$10,000 from his 401(k) into an IRA. His old employer withholds \$2,000 for federal income tax and issues Kent a check for \$8,000. Kent must come up with \$2,000 from other sources if he wants to roll over the entire \$10,000 and avoid paying tax on any of the distribution. Kent could have avoided this problem if he had elected a direct rollover option. See *Direct rollovers*, page 13-21.

## Trustee-to-Trustee Transfer

In a trustee-to-trustee transfer, funds are directly transferred from one trustee to another without ever being distributed to the participant. Because the participant never has possession of the funds, the 60-day rollover period and the 1-year waiting period rule do not apply.

**How to report a transfer.** A trustee-to-trustee transfer from one IRA to another should not be reported on Form 1099-R.

**Exception:** If the transfer is a direct rollover (described below), the transfer is reported as a rollover distribution. Form 1099-R should be issued, and the taxpayer reports the total distribution on line 4a, Form 1040, and zero on line 4b, Form 1040.

**Direct rollovers.** A transfer from the trustee of an employer qualified plan to the trustee of an IRA is called a direct rollover. The mandatory withholding rule for distributions from qualified plans does not apply to direct rollovers.

Employer qualified plans are required to give plan participants the option of having an eligible rollover distribution paid directly to a traditional IRA. This rule does not apply if the eligible rollover distribution is less than \$200.

### Transfers Incident to a Divorce

If an interest in a traditional IRA is transferred from a spouse or former spouse to a taxpayer by divorce or separate maintenance decree or a written document related to such a decree, the interest in the IRA is treated as the taxpayer's IRA starting on the date of the transfer. The transfer is tax free. The transfer can either be made by changing the name on the IRA or by making a direct transfer from the former spouse's IRA to the taxpayer's IRA.

**Distributions from a qualified plan under a divorce or similar proceeding.** The spouse or former spouse can receive a distribution from a qualified employer plan as a result of a divorce and roll a portion or all into a traditional IRA. The distribution must be one that would have been an eligible rollover distribution if it had been made to the employee and must be made under a qualified domestic relations order (QDRO). Any portion that is not rolled over is taxable; however, the 10% early withdrawal penalty does not apply. See *Qualified Domestic Relations Order (QDRO)*, page 12-11, and *Property Settlements and Transfers*, page 12-11.

**Court Case:** The taxpayer was undergoing divorce proceedings. The taxpayer took a distribution from his qualified profit-sharing plan and gave the funds to his wife, who took the funds and established an IRA within 60 days of the distribution. The lump-sum distribution was not made by reason of a qualified domestic relations order; therefore, the transfer to his wife did not qualify for tax-free rollover treatment. [*Rodoni*, 105 T.C. No. 29 (1995)]

### Disaster-Related Relief

Special rules provide for tax-favored withdrawals, repayments, extended deadlines, and loans from certain retirement plans for taxpayers who suffered economic losses as a result of certain federally-declared disasters. For information on the most recent tax relief provisions for taxpayers affected by disaster situations, go to [www.irs.gov/newsroom/tax-relief-in-disaster-situations](http://www.irs.gov/newsroom/tax-relief-in-disaster-situations). See *Qualified Disaster Recovery Distributions*, page 13-23.

## Required Minimum Distribution (RMD)

### Cross References

- Form 5329, *Additional Taxes on Qualified Plans (Including IRAs) and Other Tax-Favored Accounts*
- IRS Pub. 575, *Pension and Annuity Income*
- IRS Pub. 590-B, *Distributions from Individual Retirement Arrangements (IRAs)*

### Related Topics

- Charitable Contributions of IRA Distributions, Tab 4
- Required minimum distributions, page 29-20

## Required Minimum Distribution Rules

Taxpayers generally must begin withdrawing money from their IRA or retirement account upon reaching age 73.

**Required minimum distribution (RMD).** The RMD is the minimum amount that must be withdrawn each year.

- Taxpayers may withdraw more than the minimum required amount. See *Distributions greater than RMD*, page 13-22.
- The withdrawals will be included in taxable income except for any part that was already taxed or that can be received tax-free.

**Calculating the RMD.** The RMD for each year equals the IRA account balance as of December 31 of the preceding year, divided by the applicable distribution period, or life expectancy, for the taxpayer's age in the current tax year.

**Distribution period.** The distribution period is determined by using one of three tables.

- **Uniform Lifetime Table** (below). Use for unmarried participants and married participants whose spouse is not more than 10 years younger, or whose spouse is not the sole beneficiary of their IRA. Use actual age of participant on his or her birthday for each year.
- **Joint Life and Last Survivor Expectancy Table.** Use for married participants whose spouse is more than 10 years younger and is the sole beneficiary of their IRA. Use actual age of participant and spouse on their birthdays for each year. For table, see *Appendix B*, IRS Pub. 590-B.
- **Single Lifetime Table** (below). Use for beneficiaries who inherit a participant's IRA. Use the actual age of the beneficiary or, if there is no designated beneficiary, the participant for the first year distributions begin and then reduce by one year for each subsequent year.

**Example:** Jackie turned 75 in October 2024. Her husband Don, her sole beneficiary, turned 70 in 2024. Jackie's traditional IRA account balance on December 31, 2023, was \$100,000. Using the distribution period from the *Uniform Life Table*, below, Jackie's RMD for 2024 is \$4,065 (\$100,000 ÷ 24.6). For 2025, her RMD will be based on the account balance at the end of 2024 ÷ 23.7, her distribution period at age 76.

### Uniform Lifetime Table

Age	Distribution Period	Age	Distribution Period	Age	Distribution Period
72	27.4	80	20.2	88	13.7
73	26.5	81	19.4	89	12.9
74	25.5	82	18.5	90	12.2
75	24.6	83	17.7	91	11.5
76	23.7	84	16.8	92	10.8
77	22.9	85	16.0	93	10.1
78	22.0	86	15.2	94	9.5
79	21.1	87	14.4	95	8.9

For ages not listed in this table, see IRS Pub. 590-B for the complete table.

### Single Lifetime Table

For use by individual eligible designated beneficiaries.

Age	Distribution Period	Age	Distribution Period	Age	Distribution Period
10	74.9	23	62.1	36	49.6
11	73.9	24	61.1	37	48.6
12	72.9	25	60.2	38	47.7
13	71.9	26	59.2	39	46.7
14	70.9	27	58.2	40	45.7
15	69.9	28	57.3	41	44.8
16	69.0	29	56.3	42	43.8
17	68.0	30	55.3	43	42.9
18	67.0	31	54.4	44	41.9
19	66.0	32	53.4	45	41.0
20	65.0	33	52.5	46	40.0
21	64.1	34	51.5	47	39.0
22	63.1	35	50.5	48	38.1

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Single Lifetime Table continued

Age	Distribution Period	Age	Distribution Period	Age	Distribution Period
49	37.1	60	27.1	71	18.0
50	36.2	61	26.2	72	17.2
51	35.3	62	25.4	73	16.4
52	34.3	63	24.5	74	15.6
53	33.4	64	23.7	75	14.8
54	32.5	65	22.9	76	14.1
55	31.6	66	22.0	77	13.3
56	30.6	67	21.2	78	12.6
57	29.8	68	20.4	79	11.9
58	28.9	69	19.6	80	11.2
59	28.0	70	18.8	81	10.5

For ages not listed in this table, see IRS Pub. 590-B for the complete table.

**Distributions greater than RMD.** There is no penalty for taking distributions in excess of RMD (provided the participant is not subject to any of the early withdrawal penalties, see *Exceptions to the 10% Penalty on Early Distributions*, page 13-3). A distribution greater than the RMD cannot be carried over and used to meet the RMD for the following year.

**Required beginning date of first RMD.** The required beginning date for taxpayers is April 1 of the year following the year of the taxpayer's 73rd birthday.

**IRAs, including SEP and SIMPLE IRAs.** The first RMD must be taken by April 1 of the year following the calendar year in which the taxpayer reaches 73.

**Example:** George is retired. His 73rd birthday is on June 30, 2024. He must take his first RMD by April 1, 2025.

**Planning Tip:** The first year following the year in which the taxpayer reaches age 73 he or she will generally have two required distribution dates: April 1 for the year he or she turns 73 and December 31 for the year following. To avoid having both of these amounts included in income in the same year, the taxpayer can make the first RMD by December 31, of the year he or she turns 73 instead of waiting until April 1 of the following year.

**Qualified plans.** Qualified plans are either defined contribution plans or defined benefit plans. Examples of defined contribution plans include profit sharing plans, 401(k) plans, 403(b) plans, and money purchase plans. See *Qualified Plans*, page 13-16.

For a participant in a qualified pension plan, RMD begins by April 1 of the year following the later of the year:

- The employee turns age 73, or
- The year the employee retires.

However, even though the tax rules may permit employees to wait until retirement, some employer plans may require participants to begin to receive distributions by April 1 of the year after the year the employee turns age 73.

**5% owners.** If an employee owns more than 5% of the stock, capital, or profits interest in a company, RMDs must begin by April 1 of the year following the year the employee turns age 73.

**Roth accounts.** The RMD rules do not apply to Roth IRAs or designated Roth accounts in an employer plan. Distributions are required only after the death of the participant.

**Required date for subsequent RMDs.** For each subsequent year after the taxpayer's required beginning date, his or her RMD must be withdrawn by December 31.

**Did You Know?** A qualified longevity annuity contract (QLAC) may be held as part of an owner's IRA and will reduce the IRA value for the purpose of determining the RMD. Up to \$200,000 (2024) may be invested in the annuity contract. A QLAC pays guaranteed monthly payments starting at a future date (up to age 85). The payments are taxable when received. QLACs may be held in 401(a), 403(a), 403(b), 408 (other than a Roth IRA), or 457(b) plans.

## Penalty Tax on Excess Accumulations

The RMD rules are designed to make sure taxpayers distribute most of their retirement benefits during their lifetime, rather than passing them to beneficiaries after death.

The penalty for taking less than the RMD out of an IRA or qualified retirement plan is 25% of the part of the RMD that was not distributed during the year. The 25% excise tax is reduced to 10% if the taxpayer corrects the shortfall by submitting a return during the correction window reflecting such tax. The correction window begins on the date on which the tax is imposed and ends on the earliest of:

- The date of mailing an excise tax notice of deficiency,
- The date on which the tax imposed is assessed, or
- The last day of the second tax year that begins after the end of the tax year in which such tax is imposed.

**Form 5329, Additional Taxes on Qualified Plans (including IRAs) and Other Tax-Favored Accounts.** The penalty tax on excess accumulations is reported on Part IX, Form 5329.

**Waiver of penalty.** The penalty tax may be waived if the taxpayer establishes that the shortfall in distributions was due to reasonable error and that steps are being taken to remedy the shortfall. To request a waiver of the penalty, file Form 5329 and attach a statement of explanation.

## Inherited IRA

**Year of death.** The RMD is calculated using rules for lifetime distributions as if the owner had lived the full year. If the owner died before the required beginning date for distributions, no distribution is required for the year of death.

**Inherited IRA beneficiaries.** Generally, for IRAs inherited before 2020, beneficiaries of IRAs have fallen into two categories, individual designated beneficiaries and nondesignated beneficiaries. A designated beneficiary can be either a surviving spouse or a nonspouse individual.

**Surviving spouse designated beneficiary.** A surviving spouse who is the sole beneficiary of his or her deceased spouse's IRA may elect to be treated as the owner and not as the beneficiary. If this election is made, the taxpayer determines the RMD, if any, as if he or she was the owner beginning with the year of the election.

**Nonspouse designated beneficiary.** A nonspouse designated beneficiary is generally a child, grandchild, niece, nephew, or any other living person the account owner chooses. In general, a nonspouse designated beneficiary must take RMDs over the account owner's life expectancy (if owner died after beginning to take RMDs) or the designated beneficiary's life expectancy (stretching out the RMDs over a longer period of time).

**Stretch rule.** Generally, for accounts inherited before January 1, 2020, all individual nonspouse designated beneficiaries could stretch out the RMDs based on the beneficiary's own life expectancy. However, for accounts inherited after December 31, 2019, a 10-year rule applies for certain designated beneficiaries and only eligible designated beneficiaries can continue to use the stretch rule. See *10-year rule*, page 13-23.

**Nondesignated beneficiary.** For a nondesignated beneficiary (any nonindividual beneficiary for whom a life expectancy cannot be determined, such as a charity, the decedent's estate, or a nonqualified trust), or if a designated beneficiary is not named by September 30 of the year following the year of the IRA owner's death, RMDs are determined based on whether the decedent had begun taking RMDs yet.

- If the decedent was already receiving RMDs at the time of death, use the *Single Lifetime Table*, page 13-21, with the age of the decedent as of his or her birthday in the year of death, reduced by one for each year since the year of death.

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- If an IRA owner died prior to his or her required beginning date, the 5-year rule applies in all cases where there is no individual designated beneficiary.

**5-year rule.** The 5-year rule requires that the balance of the IRA must be withdrawn by December 31 of the year containing the fifth anniversary of the owner's death.

**10-year rule.** For accounts inherited after December 31, 2019, all distributions must be made by the end of the 10th year after the death of the decedent, except for distributions made to certain eligible designated beneficiaries.

### IRA Beneficiaries

<i>Eligible Designated Beneficiary</i>	<i>Designated Beneficiary</i>	<i>Nondesignated Beneficiary</i>
<i>(Stretch rule)</i>	<i>(10-year rule)</i>	<i>(5-year rule)</i>
<ul style="list-style-type: none"> <li>• Surviving spouse of the decedent.</li> <li>• Individual who is disabled.</li> <li>• Individual who is chronically ill.</li> <li>• Individual not more than 10 years younger than decedent (e.g., a partner, friend, sibling).</li> <li>• Minor child (not grandchild) under age 21 of decedent.*</li> </ul>	<ul style="list-style-type: none"> <li>• Nonspouse.</li> <li>• Individual who is more than 10 years younger than decedent.</li> <li>• Certain see-through trusts.</li> </ul>	<ul style="list-style-type: none"> <li>• Charities.</li> <li>• Decedent's estate.</li> <li>• Nonqualified trusts.</li> </ul>

\* A minor child ceases to be an eligible designated beneficiary as of the date the child reaches the age of majority (age 21) and any remainder of the portion of the individual's interest shall be distributed within 10 years after such date. For example, if a child inherits an IRA in the year she turns age 12, she must generally begin taking stretch RMDs beginning the following year and continue those RMDs until age 21. At that time, the 10-year rule will take effect, requiring any remaining funds in the inherited IRA to be distributed to her over the next 10 years.

**Eligible designated beneficiaries.** Eligible designated beneficiaries may still use life expectancy tables (see page 13-21) to determine RMDs (apply the stretch rule) and the 10-year rule does not apply.

**Designated beneficiaries.** Distributions to designated beneficiaries are generally required to be distributed by the end of the 10th calendar year following the year of the employee or IRA owner's death. If the decedent had begun RMDs before death, the designated beneficiary must continue RMDs (using the beneficiary's life expectancy) during the 10-year period. If the decedent did not take his or her RMD in the year of death, the beneficiary must take that RMD.

However, if the decedent had not yet reached his or her required beginning date, no RMDs are required and distributions must just be completed within 10 years after death.

**Note:** Final regulations regarding RMDs during the 10-year period were not issued until July 19, 2024 and only apply to distribution calendar years beginning on or after January 1, 2025.

**IRA with basis.** Any nondeductible contributions that gave the IRA a basis remain with the IRA after it is inherited by a beneficiary. The basis cannot be combined with the beneficiary's basis in his or her own IRAs unless the beneficiary is the decedent's spouse and chooses to treat the IRA as his or her own.

**10% early withdrawal penalty.** The 10% penalty for early withdrawal does not apply to a distribution to a beneficiary (or the estate) on or after the death of the participant [IRC §72(t)(2)(A)(ii)]. However, if a spouse chooses to roll the decedent's IRA into his or her own separate IRA, any subsequent distribution will be subject to the 10% early withdrawal penalty assuming no other exception to the penalty applies. [Gee, 127 T.C. No.1 (2006)]

**Estate tax deduction.** See *Deduction for Estate Tax Paid on IRD*, page 21-33.

## Inherited Retirement Plans

**Rollover to beneficiary.** Distributions of benefits from a deceased employee's eligible retirement plan may be rolled over directly to an IRA of a beneficiary who is not the surviving spouse of the employee [IRC §402(c)(11)]. The IRA is treated as an inherited IRA of the beneficiary. For example, distributions from the inherited IRA are subject to the distribution rules applicable to beneficiaries. The provision applies to amounts payable to a beneficiary under a qualified retirement plan, governmental section 457 plan, or a tax-sheltered annuity. To the extent provided by regulations, this rule applies to benefits payable to a trust maintained for a designated beneficiary to the same extent it applies to the beneficiary.

**Note:** A surviving spouse may roll funds from a deceased spouse's employer-sponsored pension plan or IRA over to his or her own IRA or employer-sponsored pension plan. [IRC §402(c)(9)]

## Other RMD Rules

**More than one IRA.** If a participant has more than one IRA, determine a separate RMD for each IRA based on designated beneficiaries of each IRA. However, the total RMD for all IRAs can be taken from any one or more of the IRAs.

**More than one 403(b) plan.** An owner must calculate the RMD separately for each 403(b) account, but can take the total RMD amount from one or more of the 403(b) accounts.

**More than one retirement plan.** RMDs from other types of retirement plans, such as 401(k) and 457(b) plans have to be taken separately from each of those plan accounts.

**More than one individual beneficiary.** If, as of September 30 of the year following the year an IRA participant dies, there is more than one beneficiary, the beneficiary with the shortest life expectancy is treated as the designated beneficiary if all beneficiaries are individuals, and the account or benefit has not been divided into separate accounts or shares for each beneficiary.

**Trust as beneficiary.** A trust cannot be a designated beneficiary. The beneficiaries of the trust can be treated as the designated beneficiary of the IRA if certain requirements are met.

**Rollovers.** Distributions that satisfy the RMD rules are not eligible to be rolled over.

**Annuities.** RMD rules for annuities are not the same as for IRAs. See IRS Pub. 575, *Pension and Annuity Income*, for details.

## Miscellaneous Distributions

### Cross References

- IRS Pub. 575, *Pension and Annuity Income*
- IRS Pub. 590-B, *Distributions from Individual Retirement Arrangements (IRAs)*
- IRS Pub. 721, *Tax Guide to U.S. Civil Service Retirement Benefits*

### Related Topics

- Other income, Tab 3
- Health Savings Account (HSA), page 14-6

### Qualified Disaster Recovery Distributions

Qualified disaster recovery distributions are distributions from an eligible retirement plan that are:

- Made on or after the first day of the qualified disaster,
- Made to an individual whose main home at any time during the qualified disaster was in the qualified disaster area, and
- Made to an individual who sustained an economic loss because of the disaster.

A qualified disaster for qualified disaster recovery distributions is any federally-declared disaster after December 27, 2020.

**Eligible retirement plan.** An eligible retirement plan can be any of the following:

- A qualified pension, profit-sharing, or stock bonus plan (including a 401(k) plan).
- The federal Thrift Savings Plan.
- A qualified annuity plan.
- A tax-sheltered annuity contract.
- A government section 457 deferred compensation plan.
- A traditional, SEP, SIMPLE, or Roth IRA.

**Economic loss.** Qualified disaster recovery distributions are permitted without regard to a taxpayer's need or the actual amount of his or her economic loss.

**Distribution limit.** The total of a taxpayer's qualified disaster recovery distribution from all plans is limited to \$22,000 per disaster. If a taxpayer takes distributions from more than one type of plan, and the total amount of his or her distributions exceeds \$22,000 for a single disaster, he or she may allocate the \$22,000 limit among the plans by any reasonable method.

**Taxation of qualified disaster recovery distributions.** Qualified disaster recovery distributions are included in income in equal amounts over three years. However, a taxpayer can elect to include the entire distribution in his or her income in the year it was received.

Qualified disaster recovery distributions are not subject to the 10% additional tax (or the 25% tax for certain distributions from SIMPLE IRAs) on early distributions from qualified retirement plans (including IRAs). Also, if a taxpayer is receiving substantially equal periodic payments from a qualified retirement plan, the receipt of a qualified disaster recovery distribution from that plan will not be treated as a change in those substantially equal payments merely because of that distribution. Any distributions in excess of the \$22,000 qualified disaster recovery distribution limit may be subject to the additional tax on early distributions.

**Repayment of qualified disaster recovery distributions.** The taxpayer has three years from the day after the date he or she received the qualified disaster recovery distribution to make a repayment. The amount of repayment cannot be more than the amount of the original distribution. Amounts that are repaid are treated as trustee-to-trustee transfers and are not included in income. Also, for purposes of the one-rollover-per-year limitation for IRAs, a repayment to an IRA is not considered a rollover.

**Exceptions.** A taxpayer cannot repay the following types of distributions:

- Qualified disaster recovery distributions received as a beneficiary (other than as a surviving spouse).
- Required minimum distributions.
- Periodic payments (other than from an IRA) that are for:
  - A period of 10 years or more,
  - The joint lives or joint life expectancies of the taxpayer and his or her beneficiary.

**Repayment of distributions if reporting under the one-year election.** If a taxpayer elects to include all of the qualified disaster recovery distributions received in a year in income for that year and then repay any portion of the distribution during the allowable three-year period, the amount repaid will reduce the amount included in income for the year of distribution. If the repayment is made after the due date (including extensions) for the return for the year of distribution, the taxpayer will need to file an amended return.

**Repayment of distributions if reporting under the three-year method.** If a taxpayer is reporting the qualified disaster recovery distribution in income over a three-year period and repays any portion of the distribution to an eligible retirement plan before filing his or her current year tax return, the repayment will reduce the portion of the distribution that is included in income. If the

taxpayer repays a portion after the due date (including extensions) for filing his or her current year return, the repayment will reduce the portion of the distribution that is included in income on his or her following year return, unless the taxpayer is eligible to amend his or her prior year returns as applicable. If, during a year in the three-year period, the taxpayer repays more than is otherwise includible in income for that year, the excess may be carried forward or back to reduce the amount included in income for the year.

**Reporting distributions and repayments.** To report qualified disaster recovery distributions and repayments, use Form 8915-F, *Qualified Disaster Retirement Plan Distributions and Repayments*.

## Pension Plans of Public Safety Employees

The 10% early withdrawal penalty does not apply to distributions from a governmental qualified retirement plan to qualified public safety employees or private sector firefighters who separate from service after age 50 or 25 years of service under the plan, whichever is earlier.

A qualified public safety employee is any state or local employee that provides police protection, firefighting services, emergency medical services, services as a corrections officer or as a forensic security employee providing for the care, custody, and control of forensic patients, or any federal law enforcement officer, federal customs and border protection officer, federal firefighter, air traffic controller, nuclear materials courier, member of the U.S. Capital Police, member of the Supreme Court police, or any diplomatic security special agent of the Department of State.

See *Exceptions to the 10% Penalty on Early Distributions—Code 01*, page 13-3.

## Qualified HSA Funding Distribution (QHFD)

A one time, tax-free, distribution is allowed from an individual's Roth or traditional IRA to fund his or her health savings account (HSA). The distribution must be a trustee-to-trustee transfer. The amount distributed and amounts otherwise contributed are subject to HSA annual funding limits. Distributions are taken first from tax deferred income. See *Qualified HSA funding distribution*, page 30-9.

## Qualified Reservist Distribution

An individual who receives a qualified reservist distribution may, at any time during the 2-year period, beginning on the day after the end of the active duty period, make one or more contributions to an IRA in an amount not to exceed the amount of the qualified reservist distribution. The IRA contribution limitations otherwise applicable do not apply, and no deduction is allowed for the contribution under this rule. See *Exceptions to the 10% Penalty on Early Distributions—Code 11*, page 13-3.

## Domestic Abuse Distribution

**New for 2024** A distribution to a domestic abuse victim is not subject to the 10% additional tax on early distributions if the distribution is made from an applicable eligible retirement plan and made to an individual during the 1-year period beginning on the date on which the individual is a victim of domestic abuse by a spouse or domestic partner. See *Exceptions to the 10% Penalty on Early Distributions – Code 22*, page 13-3.

An eligible distribution to a domestic abuse victim must not exceed the lesser of \$10,000 or 50% of the present value of the nonforfeit-able accrued benefit of the employee under the plan. The distribution may be repaid at any time during the 3-year period beginning on the day after the date on which the distribution was received.

**Eligible retirement plan.** An applicable eligible retirement plan is any of the following:



- IRA.
- Individual retirement annuity.
- Qualified trust.
- 403(a) annuity plan.
- Qualified annuity plan.
- 457(b) deferred compensation plan.
- 403(b) annuity contract.

An applicable eligible retirement plan does not include a defined benefit plan or a joint and survivor annuity.

## Emergency Personal Expense Distribution

**New for 2024** An exception to the 10% penalty on early distributions applies to withdrawals for the purposes of meeting unforeseeable or immediate financial needs relating to necessary personal or family emergency expenses. See *Exceptions to the 10% Penalty on Early Distributions – Code 23*, page 13-3.

Not more than one distribution per calendar year may be treated as an emergency personal expense distribution. The distribution is limited to the lesser of \$1,000 or an amount equal to the excess of:

- 1) The individual's total non-forfeitable accrued benefit under the plan (the individual's total interest in the plan in the case of an individual retirement plan), determined as of the date of each such distribution, over
- 2) \$1,000.

**Repayment.** An individual may repay the distribution back into the plan within three years of the distribution, which in turn treats the distribution as either a trustee-to-trustee transfer, or as rollover, and thus avoid paying regular tax on the distribution.

**Limit on subsequent distributions.** If a taxpayer takes an emergency personal expense distribution during a tax year, no amount may be treated as an emergency personal expense distribution during the immediately following three calendar years, unless the previous distribution is fully repaid, or the aggregate of the elective deferrals and employee contributions to the plan subsequent to the previous distribution is at least equal to the amount of the previous distribution.

## Foreign Pension and Annuity Distributions

### Cross References

- Form 3520, *Annual Return To Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts*
- Form 3520-A, *Annual Information Return of Foreign Trust With a U.S. Owner*
- Form 8938, *Statement of Specified Foreign Financial Assets*
- IRS Pub. 54, *Tax Guide for U.S. Citizens and Resident Aliens Abroad*
- IRS Pub. 519, *U.S. Tax Guide for Aliens*
- IRS Pub. 901, *U.S. Tax Treaties*

### Related Topics

- Other income, Tab 3

### Foreign Pension and Annuity Distributions

A foreign pension or annuity distribution is a payment from a pension plan or retirement annuity received from a source outside the U.S. A taxpayer might receive one from a:

- Foreign employer.
- Trust established by a foreign employer.
- Foreign government or one of its agencies (including a foreign Social Security pension).
- Foreign insurance company.
- Foreign trust or other foreign entity designated to pay the annuity.

Similar to U.S. pensions or annuities, the taxable amount generally is the gross distribution minus the basis (investment in the contract). Income received from foreign pensions or annuities may be fully or partially taxable, even if the taxpayer does not receive a Form 1099 or similar document reporting the amount of income.

**Treaty benefits.** As a general rule, the pension/annuity article of most income tax treaties allows for exclusive taxation of pensions or annuities under the domestic law of the resident country. This is generally true unless a treaty provision specifically amends that treatment. For example, some treaties provide that the country of residence may not tax amounts that would not have been taxable by the other country if you were a resident of that country. There also may be special rules for lump-sum distributions.

**Government pensions.** With respect to government pensions/public pensions/annuities (typically covered under the Government Service article) or Social Security payments, generally the payments are only taxable by the country in which the government is making the payments. Note that what constitutes a government pension or public pension is dictated by the treaty, and the rule may apply narrowly.

**Taxpayer residing in a foreign country.** If the taxpayer resides in a foreign country and receives a pension/annuity paid by a U.S. payor, the taxpayer may claim an exemption from withholding of U.S. federal income tax under a tax treaty by completing Form W-8BEN, *Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding and Reporting*, and delivering it to the U.S. payor. The taxpayer must report his or her U.S. taxpayer identification number (TIN) on Form W-8BEN for it to be valid for treaty purposes.

**Taxpayer residing in the U.S.** If the taxpayer lives in the United States and receives a pension/annuity paid by a foreign payor, he or she must claim the appropriate treaty withholding exemption on the form, and in the manner specified by the foreign government. If the foreign government, and/or the foreign withholding agent, refuses to honor the treaty claim, make the treaty claim on the taxpayer's income tax return, or other prescribed form, filed with the foreign country. Additionally, the taxpayer may be able to claim a foreign tax credit on his or her U.S. federal individual income tax return for any foreign income tax withheld from his or her foreign pension or annuity. A foreign tax credit generally would not be permitted for tax withheld that is in excess of the liability under foreign law, taking into consideration applicable income tax treaties. See *Foreign Tax Credit*, page 11-11.

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**Author's Comment:** Read each treaty's relevant articles in their entirety as there may be special provisions which affect the taxability of income. In addition, read any Protocols (amendments) to the treaty as they may revise the relevant articles of the treaty and affect eligibility for benefits or the taxability of income. The Technical Explanation accompanying the treaty may also provide insight, in particular, with respect to what meets the treaty's definition of a pension, public pension, or a pension paid in connection with government service. Each treaty should be looked at carefully as benefits vary from treaty to treaty—just because one treaty allows a certain treatment does not mean another treaty will allow the same treatment.

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**Foreign Social Security pensions.** Foreign Social Security pensions are generally taxed as if they were foreign pensions or foreign annuities. They are not eligible for exclusion from taxable income the way a U.S. Social Security pension might be unless a tax treaty provides for an exclusion.

Most income tax treaties have special rules for Social Security payments. Generally, U.S. treaties provide that Social Security payments are taxable by the country making the payments. However, a foreign Social Security payment may also be taxable in the U.S. if the taxpayer is a U.S. citizen or resident.

**Foreign government pensions.** Many U.S. tax treaties provide that a pension received for government services will only be taxable by the payor country if the person is a citizen/national of the country to which government services are provided and is not a citizen or green card holder in the country where the services were performed.

**Foreign employer contributions.** If a taxpayer worked abroad, his or her basis might include amounts contributed by his or her employer that were not includible in his or her gross income. This applies to contributions made either:

- Before 1963 by the taxpayer's employer for the work abroad,
- After 1962 by the taxpayer's employer for the work abroad if the taxpayer performed the services under a plan that existed on March 12, 1962, or
- After 1996 by the taxpayer's employer on his or her behalf if he or she was a foreign missionary (a duly ordained, commissioned, or licensed minister of a church or a lay person).

**Foreign contributions while a nonresident.** A taxpayer's contributions and his or her employer's contributions are not part of the taxpayer's basis if the contribution was based on compensation for services performed outside the U.S. while the taxpayer was a nonresident and not subject to income tax under the laws of the U.S. or any foreign country (but only if the contribution would have been taxable if paid as cash compensation when the services were performed).

**Treaty benefits for pension contributions.** There are relatively few U.S. treaties which provide benefits for cross border pension contributions. Benefits may allow a U.S. citizen that is a resident in a foreign country to obtain favorable tax treatment in the foreign country for contributions made to a U.S. pension plan or may allow a U.S. citizen that is a resident in a foreign country to obtain favorable tax treatment in the U.S. for a contribution made to a foreign pension plan.

## Social Security

### Cross References

- Social Security online, [www.ssa.gov](http://www.ssa.gov)
- Social Security contact number, 1-800-772-1213, TTY 1-800-325-0778

### Related Topics

- Social Security Lump-Sum Repayments, Tab 3
- Self-Employment Tax, Tab 5
- Federal Insurance Contributions Act (FICA), page 23-4

### Social Security Basics

**Social Security card—applications, replacements, and changes.** To apply for a Social Security Number, replace a card, or change information on the card, complete Form SS-5, *Application for Social Security Card*, and send along with original documents to the local Social Security office.

- To apply for a Social Security Number, provide original documents proving U.S. citizenship or immigration status, age, and identity.
- To replace a lost or stolen Social Security card, submit a recently issued document proving identity. The replacement card will have the same name and number as the previous card.
- To change information on a Social Security card, send proof of identity and documents supporting the change (e.g. a birth certificate, a marriage certificate, or divorce decree).

**Note:** Form SS-5 is available at [www.ssa.gov/forms](http://www.ssa.gov/forms).

**Help for domestic violence victims.** A new Social Security Number may be assigned when evidence shows a person is being harassed, abused, or his or her life is endangered. Application must be made in person at a Social Security office.

**Document requirements for application.** Any required documents must be originals or copies certified by the custodian of record. Photocopies or notarized copies are not accepted. Originals are returned after verification.

**Social Security statement.** A Social Security statement is a record of earnings on which a worker has paid Social Security taxes during his or her working years, and a summary of the estimated benefits the worker and family members may receive as a result of those earnings.

Taxpayers can access their individual statement online at [www.ssa.gov/myaccount](http://www.ssa.gov/myaccount). The individual must first go online and create a *my Social Security* account after which he or she will be able to access a personalized statement at any time.

**Mailing of statements.** Social Security statements are mailed to workers age 60 and older who are not currently receiving Social Security benefits and do not yet have a *my Social Security* account. The statement is mailed three months prior to the taxpayer's birthday.

**How to qualify for benefits.** When an individual works and pays Social Security taxes, he or she earns credits toward Social Security benefits. The number of credits needed to get benefits depends on when the individual was born. If the individual stops working before he or she has enough credits to qualify for benefits, the credits will remain on his or her Social Security record. Upon returning to work, the individual can add more credits. No benefits can be paid until the required number of credits has been reached.

**Amount of earnings needed to earn one quarter of coverage.** A worker receives one credit for each \$1,730 earned in 2024. The amount of earnings needed for a quarter of coverage increases automatically each year. A maximum of four credits may be earned in any given year.

**Retirement benefits.** Anyone born after 1929 needs a minimum of 10 years of work (40 credits) to be eligible for retirement benefits.

**Disability benefits.** To qualify for disability benefits, a taxpayer must meet two earnings tests.

- 1) Recent work test, and
- 2) Duration of work test.

**Recent work test.** The taxpayer must have worked a certain number of quarters in the most recent years before disability.

If worker became disabled:	Then worker generally needs:
In or before the quarter the worker turns age 24.	1½ years of work (6 credits) during the three-year period ending with the quarter in which the worker became disabled.
In the quarter after the worker turns age 24, but before the quarter in which he or she turns age 31.	Work during half the time for the period beginning with the quarter after worker turned age 21 and ending with the quarter in which the worker became disabled.*
In the quarter the worker turns age 31 or later.	Five years of work (20 credits) out of the 10-year period ending with the quarter in which the worker became disabled.

\* **Example:** If a worker becomes disabled in the quarter he turned age 27, then he would need three years of work (12 credits) out of the six-year period ending with the quarter he became disabled.

**Duration of work test.** The taxpayer must have worked a certain number of years during his or her lifetime.

Disabled at Age	Years Needed	Disabled at Age	Years Needed
Before 28	1½ yrs	48	6½ yrs
30	2 yrs	50	7 yrs
34	3 yrs	52	7½ yrs
38	4 yrs	54	8 yrs
42	5 yrs	56	8½ yrs
44	5½ yrs	58	9 yrs
46	6 yrs	60	9½ yrs

**Note:** For illustration purposes only. This table does not cover all situations.

**Survivor's benefits.** When a worker who has paid Social Security taxes dies, certain members of the family may be eligible for survivor's benefits. Survivors of a young worker who has died may be eligible for benefits if the deceased worker was employed for at least 1½ years during the three years before his or her death. Survivor's benefits may be paid to:

- A surviving spouse: 100% of deceased spouse's benefit at full retirement age, or reduced benefits as early as age 60.
- A disabled surviving spouse: As early as age 50.
- A surviving spouse of any age who takes care of the decedent's child who is under age 16 or disabled and receiving Social Security benefits.
- Unmarried children under age 18, or up to age 19 if they attend high school full time. Under certain circumstances, benefits can be paid to stepchildren, grandchildren, or adopted children.
- Children who were disabled before age 22 and remain disabled.
- Dependent parents age 62 or older if the worker provided at least one-half of their support.

**Family benefits.** For a worker collecting Social Security who is still alive, the following family members may also receive benefits.

- A spouse age 62 or older,
- A spouse younger than 62, if he or she is taking care of their child entitled on the worker's record who is under age 16 or disabled,
- A former spouse age 62 or older (see *Benefits for divorced people*, below),
- Children up to age 18, or 19 if they are full-time students who have not yet graduated from high school, and
- Children who are disabled, even if they are age 18 or older.

**Spouse's benefits.** A spouse who has not worked, or who has low earnings, can be entitled to as much as 50% of the retired worker's full benefit. If a spouse is entitled to both his or her own retirement benefits, and for benefits as a spouse, the spouse's own benefits will always be paid first. If the benefits as a spouse are higher, then retirement benefits will be a combination of benefits equaling the higher spouse benefit.

**Note:** A taxpayer's current spouse cannot receive spouse's benefits until the taxpayer files for retirement benefits.

**Deemed filing.** Taxpayers who make a claim for benefits at full retirement age will be "deemed" to apply for both their own and spousal benefits. Deemed filing rules also apply to all applicants below full retirement age, but do not apply to spouses with children or who are disabled.

**Benefits for divorced people.** In order to qualify for divorced spousal benefits, the spouse must:

- Have been married to their ex-spouse for at least 10 years,
- Be at least age 62 or older,
- Be unmarried,
- Not be eligible for an equal or higher benefit under his or her own Social Security record or on someone else's Social Security record, and
- Be entitled to Social Security retirement or disability benefits.

**Note:** The amount of benefits the divorced spouse gets has no effect on the amount of benefits the worker or the worker's current spouse may receive.

## Earnings Records

Social Security benefits are based upon an individual's earnings as reported to the Social Security Administration (SSA). These earnings are used to determine whether an individual is eligible for retirement, survivors, disability, and health insurance benefits. They are also used to calculate cash benefit rates.

An individual's earnings record shows the amount of earnings reported by his or her employer or by the individual, if self-employed. It also shows the periods for which the earnings were reported.

**Employees.** Reports of earnings must be filed annually with SSA by every employer who:

- Is required to withhold income tax from wages, and/or
- Is liable for Federal Insurance Contributions Act (FICA) taxes (also known as Social Security and Medicare taxes).

An individual's Social Security and Medicare taxes are deducted when wages are paid and reported to the employee annually on Form W-2, *Wage and Tax Statement*.

**More than one employer.** If an individual works for more than one employer, he or she may not owe all the taxes deducted by the employers. The tax is deducted on wages paid by each employer up to the maximum wages creditable for Social Security. Therefore, the total deducted may be more than the individual owes. Any excess may be claimed as a credit against the individual's income tax when filing his or her income tax return for that year.

See *Excess Social Security and RRTA Tax Withheld*, Tab 3.

**Self-employed.** A self-employed individual must pay self-employment tax on net earnings of \$400 or more. Self-employment tax is comprised of Social Security and Medicare tax and is similar to FICA taxes withheld from the pay of most wage earners.

**Self-employment tax.** Social Security taxes are paid on self-employment income up to the maximum amount creditable for the year. Medicare taxes are paid on all self-employment income as there is no yearly maximum.

**Partnership earnings.** A partner in a partnership should include his or her share of the partnership net earnings or loss from self-employment on his or her individual tax return.

## Taxable Social Security Benefits

A portion of Social Security retirement and disability benefits may be taxable when income exceeds a taxpayer's base amount. Certain amounts that are nontaxable for regular income tax purposes are added back to determine taxable Social Security benefits. The base amount is determined by the taxpayer's filing status.

### Taxable Social Security Benefits Base Amounts

MFJ	\$32,000
Single, HOH, QSS, MFS (lived apart from spouse all year)	\$25,000
MFS (lived with spouse at any time during the year)	\$0

**Rate of taxation.** Income above a taxpayer's base amount will result in an inclusion of up to 50% (85% for higher incomes) of the taxpayer's Social Security benefits on line 6b, Form 1040.

**Social Security benefits for children.** Taxable Social Security benefits are included in income of the person who has the legal right to receive the benefits. For example, if a parent and the parent's child both receive benefits, but the check for the child's benefit is made out in the parent's name, use only the parent's part of the benefits to determine whether any benefits are taxable on the parent's tax return. One-half of the part that belongs to the child must be added to the child's other income to determine whether any of those benefits are taxable on the child's tax return.

**Repayment of Social Security benefits.** Any repayment of benefits made during the year (even if for an earlier year) must be subtracted from gross benefits received. Gross benefits are shown in box 3 of Form SSA-1099, *Social Security Benefit Statement*, or Form RRB-1099, *Payments by the Railroad Retirement Board*. Repayments are shown in box 4 of these forms. The amount in box 5 shows net benefits for the year (box 3 minus box 4). Use the amount in box 5 to determine whether any of the benefits are taxable.

## How Benefits Are Calculated

The amount of Social Security retirement benefits is based on:

- Lifetime earnings, and
- Age at time of retirement.

**Lifetime earnings.** Higher lifetime earnings result in higher benefits. The highest 35 years are used to calculate average monthly earnings. Each year is indexed for inflation to approximate what earnings for that year would be in today's dollars. Earnings for each year are also capped by the Social Security maximum earnings subject to Social Security tax for that year. After calculating the average indexed monthly earnings, a formula is used to determine the primary insurance amount (PIA).

### Computation of the PIA for Person First Eligible in 2024

	Average indexed monthly earnings
90% of the first.....	\$1,174 plus
32% of the amount between.....	\$1,174 and \$7,078 plus
15% of the amount over.....	\$7,078

**Example:** Michael retired in 2024 when he turned age 66 and 8 months. He had average indexed monthly earnings of \$8,000 based on his highest earning 35 years.

1) 90% × \$1,174	=	\$1,056.60
2) 32% × (\$7,078 – \$1,174)	=	1,889.28
3) 15% × (\$8,000 – \$7,078)	=	138.80
Total monthly benefit	=	\$3,084.18

**Note:** The maximum monthly benefit for 2024 is \$3,822, regardless of income. See *Social Security and Medicare Highlights*, page 13-1.

For the family of a worker who turns age 62, or dies in 2024 before attaining age 62, the maximum amount of benefits that can be paid is computed as follows.

- 150% of the first \$1,500 of the worker's PIA, plus,
- 272% of the worker's PIA over \$1,500 through \$2,166, plus,
- 134% of the worker's PIA over \$2,166 through \$2,825, plus,
- 175% of the worker's PIA over \$2,825.

A worker who qualifies for disability benefits will generally receive 100% of PIA, provided enough work credits are earned before becoming disabled.

**Age at time of retirement.** The amount of benefits also depends on the age when a person decides to start collecting Social Security.

**Full retirement age.** Full retirement age is the age at which retirement benefits equal 100% of PIA. See *Full Retirement Age* chart, below, for full retirement age based on birth year.

### Full Retirement Age

#### Workers and Spouses

Birth Date	Full Retirement Age (FRA)	Birth Date	Full Retirement Age (FRA)
Prior to 1/2/1938	65 yrs	1/2/1955–1/1/1956	66 yrs, 2 mo.
1/2/1938–1/1/1939	65 yrs, 2 mo.	1/2/1956–1/1/1957	66 yrs, 4 mo.
1/2/1939–1/1/1940	65 yrs, 4 mo.	1/2/1957–1/1/1958	66 yrs, 6 mo.
1/2/1940–1/1/1941	65 yrs, 6 mo.	1/2/1958–1/1/1959	66 yrs, 8 mo.
1/2/1941–1/1/1942	65 yrs, 8 mo.	1/2/1959–1/1/1960	66 yrs, 10 mo.
1/2/1942–1/1/1943	65 yrs, 10 mo.	1/2/1960 and later	67 yrs
1/2/1943–1/1/1955	66 yrs		

Surviving Spouse(s)			
Birth Date	Full Retirement Age (FRA)	Birth Date	Full Retirement Age (FRA)
1/2/1940–1/1/1941	65 yrs, 2 mo.	1/2/1957–1/1/1958	66 yrs, 2 mo.
1/2/1941–1/1/1942	65 yrs, 4 mo.	1/2/1958–1/1/1959	66 yrs, 4 mo.
1/2/1942–1/1/1943	65 yrs, 6 mo.	1/2/1959–1/1/1960	66 yrs, 6 mo.
1/2/1943–1/1/1944	65 yrs, 8 mo.	1/2/1960–1/1/1961	66 yrs, 8 mo.
1/2/1944–1/1/1945	65 yrs, 10 mo.	1/2/1961–1/1/1962	66 yrs, 10 mo.
1/2/1945–1/1/1957	66 yrs	1/2/1962 and later	67 yrs

**Early retirement age.** If benefits begin prior to full retirement age, benefits are permanently reduced. See *Early Retirement Reduced Benefits* chart, below, for the reduction of benefits when Social Security benefits begin at age 62.

### Early Retirement Reduced Benefits

The earliest age a person can begin receiving Social Security benefits is age 62. The following table illustrates the effect on a primary beneficiary's benefit, and a spouse's benefit (who receives 50% of the primary beneficiary's PIA) when Social Security benefits begin at age 62.

Year of Birth	Primary's Reduction Percentage	Spouse's Reduction Percentage
1943 – 1954	25.00%	30.00%
1955	25.83%	30.83%
1956	26.67%	31.67%
1957	27.50%	32.50%
1958	28.33%	33.33%
1959	29.17%	34.17%
After 1959	30.00%	35.00%

**Benefits begin after full retirement age.** If benefits begin after full retirement age, benefits are permanently increased. By delaying the age at which a person begins to receive Social Security, benefits may increase under one of the following conditions.

- Each year a person works adds another year of earnings to their Social Security record, which may result in higher lifetime earnings upon which benefits are based, or
- Benefits increase automatically by a certain percentage from the time a person reaches full retirement age until the start of receiving Social Security benefits. The percentage varies depending on the year of birth. For example, a person born in 1943 or later will receive an 8% per year increase (until age 70) in benefits for each year that signing up for Social Security is delayed.

**Note:** Even if a person decides to delay receiving Social Security benefits, signing up for Medicare benefits must still be done at age 65. Medical insurance costs may increase if there is a delay in signing up for Medicare past age 65. See *Eligibility*, page 13-29.

## How Work Affects Retirement Benefits

A person can receive Social Security retirement or survivors benefits and work at the same time. However, benefits could be reduced if earnings exceed certain amounts. Different rules apply to Social Security recipients who are disabled and who continue to work.

**Work after reaching full retirement age.** A worker can keep all Social Security benefits received no matter how much they earn once they reach full retirement age.

**Work before reaching full retirement age.** If a worker receiving Social Security benefits has not reached full retirement age by the end of 2024, benefits are reduced by \$1 for each \$2 earned above \$22,320 during 2024.

**Example:** Howard is age 63. He has not reached full retirement age. In addition to his \$1,400 (\$16,800 annually) monthly Social Security benefits, he receives \$1,910 (\$22,920 annually) in earnings from work. His earnings are \$600 over the \$22,320 limit. He is still eligible to receive \$22,020 in benefits during the year (\$22,320 minus \$300).

**Work during year of reaching full retirement age.** If a worker receiving Social Security benefits reaches full retirement age during 2024, benefits are reduced by \$1 for each \$3 earned above \$59,520 until the month the worker reaches full retirement age.

**Example:** Arne is eligible for \$600 per month in Social Security benefits for all of 2024, but will not reach full retirement age until September 2024. He will earn \$60,520 in the eight months from January through August, which is \$1,000 above the \$59,520 limit. During the eight-month period, Arne's benefits are reduced by \$333 ( $\$1,000 \div 3$ ). Arne will still be eligible to receive \$4,467 of Social Security benefits for the first eight months of 2024 ( $\$600 \times 8 = \$4,800 - \$333 = \$4,467$ ). Starting in September, when Arne reaches full retirement age, he will be eligible to receive his full benefits no matter how much he earns.

**Work during first year of early retirement.** If an individual is younger than full retirement age and has earnings above the limit for the year, the person may retire and be eligible for benefits if monthly earnings are less than \$1,860 (2024) and the retiree is not self-employed.

**Example:** John retired at age 62 on October 31, 2024. He made \$45,000 through October 2024. Beginning in November, he took a part-time job earning \$500 per month. Although his earnings for the year were substantially higher than the 2024 limit of \$22,320, he was entitled to receive a Social Security payment for November and December. This is because his earnings in those months were less than \$1,860. If John earned more than \$1,860 in either November or December, he would not be entitled to receive a benefit for that month. Beginning in 2025, only the annual limit applies to John because he is beyond his first year of retirement.

**What income counts?** Only Form W-2 wages and self-employment income count toward the Social Security earnings limit. Income from government benefits, investment earnings, interest, pensions, annuities, and capital gains does not count. For Form W-2 wages, income counts when it is earned, not when it is paid. For self-employment earnings, income counts when it is received, not when it is earned, unless it is paid in a year after the self-employed person becomes entitled to Social Security, and it was earned before the person became entitled.

**Reporting earnings.** Benefits are adjusted based on estimated earnings for the year. If at any time during the year a recipient sees that earnings will be different from the estimated amount reported, call Social Security to revise the estimate.

### Supplemental Security Income (SSI)

SSI makes monthly payments to people who have low income and few resources and are age 65 or older, blind, or disabled. SSI is not taxable. The monthly maximum benefits for 2024 are:

- Individual: \$943.
- Married couple: \$1,415.

## Medicare

### Cross References

- Medicare online, [www.medicare.gov](http://www.medicare.gov)
- Medicare contact number, 1-800-633-4227 or 1-800-MEDICARE

### Related Topics

- Medical Expenses, page 4-2
- Payroll and Labor Laws, Tab 23

### Medicare Basics

- People age 65 and older.
- People of all ages with certain disabilities, permanent kidney failure, or amyotrophic lateral sclerosis (ALS).

**Deducting Medicare costs.** Medicare insurance premiums for Medicare Parts A, B, C, and D, as well as any Medigap premiums, are allowable as itemized deductions on Schedule A (Form 1040). See *Medical Expenses*, page 4-2.

#### Medicare Basic Coverage

Original Medicare Plan Part A (Hospital) Part B (Medical)	or	Medicare Advantage Plans like HMOs and PPOs Called "Part C," this option combines Part A (Hospital) and Part B (Medical);
Medicare provides this coverage. Part B is optional. The individual has choice of doctors. Costs may be higher than in Medicare Advantage Plans.		Private insurance companies approved by Medicare provide this coverage. Generally, doctors must be in the plan. Costs may be lower than in the Original Medicare Plan, and extra coverage (like vision, hearing, and dental) may be available. Copayment or coinsurance payments may apply. Plans have a yearly limit on out-of-pocket costs.
<b>Medigap (Medicare Supplement Insurance Policy)</b> The individual can choose to buy this private coverage (or an employer/union may offer similar coverage) to fill in gaps in Part A and Part B coverage. Costs vary by policy and company.		
<b>Plus</b>		<b>Plus</b>
<b>Part D (Prescription Drug Coverage)</b> Optional coverage. Private companies approved by Medicare run these plans. Plans cover different drugs. Medically necessary drugs must be covered.		<b>Part D (Prescription Drug Coverage)</b> Most Part C plans cover prescription drugs. If they do not, this coverage may be available separately. Plans cover different drugs. Medically necessary drugs must be covered.

**Eligibility.** Taxpayers are first eligible to join Medicare during the period that begins three months before age 65 and ends three months after the month the individual turns 65. If the taxpayer receives Medicare due to a disability, he or she can join three months before or after his or her 24th month of disability.

#### Medicare Eligibility

Hospital Insurance (Part A)	
	Citizens or permanent residents of the United States are eligible for free Medicare Part A if age 65 or older and: <ul style="list-style-type: none"> <li>• Taxpayer receives or is eligible to receive Social Security benefits or railroad retirement benefits, or</li> <li>• Taxpayer or spouse (living or deceased, including divorced spouses) worked long enough in a government job where Medicare taxes were paid, or</li> <li>• Taxpayer is the dependent parent of a fully insured deceased child.</li> </ul>
	Before age 65, eligible for free Medicare Part A if: <ul style="list-style-type: none"> <li>• Taxpayer has been entitled to Social Security disability benefits for 24 months, or</li> <li>• Taxpayer receives a disability pension from RRB, or</li> <li>• Taxpayer receives Social Security benefits due to ALS, or</li> <li>• Taxpayer (or is the child or surviving spouse of someone who) worked long enough in a government job where Medicare taxes were paid and meets the requirements of the Social Security disability program, or</li> <li>• Taxpayer has permanent kidney failure and receives maintenance dialysis or a kidney transplant and meets certain conditions.</li> </ul>
	<b>Not eligible for Part A.</b> If a taxpayer does not qualify, he or she may be able to get Medicare Part A by signing up during designated enrollment periods and paying a monthly premium.

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<i>Medicare Eligibility continued</i>	
<b>Medical Insurance (Part B)</b>	<p>Anyone eligible for Part A can also enroll in Part B by paying a monthly premium.</p> <p>If a taxpayer is not eligible for free Medicare Part A, he or she can buy Part B, without having to buy Part A, if taxpayer is age 65 or older and a:</p> <ul style="list-style-type: none"> <li>• U.S. citizen, or</li> <li>• Lawfully admitted noncitizen who has lived in the United States for at least five years.</li> </ul>
<b>Medicare Advantage Plans (Part C)</b>	<p>Taxpayers who have Medicare Parts A and B can join a Medicare Advantage Plan (Part C). With one of these plans, a taxpayer does not need a Medigap policy. Medicare Advantage Plans include:</p> <ul style="list-style-type: none"> <li>• Medicare Health Maintenance Organization (HMO) Plans,</li> <li>• Medicare Preferred Provider Organization (PPO) Plans,</li> <li>• Medicare Private Fee-For-Service (PFFS) Plans, and</li> <li>• Medicare Special Needs Plans (SNPs).</li> </ul> <p>Medicare Advantage Plans may require a monthly premium.</p>
<b>Medicare Prescription Drug Plans (Part D)</b>	<p>Taxpayers who have Medicare Part A, Part B, or Part C, are eligible for prescription drug coverage (Part D). Joining a Medicare prescription drug plan is voluntary, and includes an additional monthly premium for coverage.</p> <p>Taxpayers may be subject to a penalty for waiting to enroll in Part D if current prescription drug coverage is not at least as good as Medicare prescription drug coverage.</p>

## Medicare Part A Premiums

Most people do not pay for Part A because they or their spouse had more than 40 quarters of Medicare-covered employment. However, those who have less than 40 quarters of Medicare-covered employment, pay up to \$505 each month in 2024.

## Medicare Part B Premiums

Anyone who is eligible for Medicare Part A can enroll in Medicare Part B by paying a monthly premium. Beneficiaries with higher incomes will pay higher premiums. Income used to determine the 2024 Medicare Part B premium is taken from an individual's 2022 tax return. If income has decreased since 2022, the individual can contact Social Security and ask for a redetermination.

### 2024 Medicare Part B Monthly Premium

<i>Modified AGI for Single, HOH, QSS (2022 Return)</i>	<i>Modified AGI for MFJ (2022 Return)</i>	<i>Monthly Premium for Each Person</i>
Up to \$103,000	Up to \$206,000	\$174.70
\$103,001 to \$129,000	\$206,001 to \$258,000	\$244.60
\$129,001 to \$161,000	\$258,001 to \$322,000	\$349.40
\$161,001 to \$193,000	\$322,001 to \$386,000	\$454.20
\$193,001 to \$499,999	\$386,001 to \$749,999	\$599.00
Over \$499,999	Over \$749,999	\$594.00
<i>Modified AGI for MFS (2022 Return)</i>	<i>Monthly Premium for Each Person</i>	
Up to \$103,000	\$174.70	
\$103,001 to \$396,999	\$599.00	
Over \$396,999	\$594.00	

**Note:** Modified AGI is AGI plus tax-exempt interest.

The standard Part B premium amount in 2024 is \$174.70 (or higher depending on 2022 income). A small number of participants will pay less if the increase in Social Security benefits for the year has been insufficient to cover the rising cost of Medicare premiums.

An individual pays the standard premium amount (or higher) if he or she:

- Enrolls in Medicare Part B for the first time in 2024,
- Does not get Social Security benefits,
- Is directly billed for Medicare Part B premiums,
- Has Medicare and Medicaid, and Medicaid pays the premiums, or
- Pays an additional income-related premium.

**Part B deductible.** The Medicare Part B deductible is \$240 (2024). After the deductible is met, an individual typically pays 20% of the Medicare-approved amount for most doctor services, outpatient therapy, and durable medical equipment.

## Medicare Part C Coverage

Medicare Advantage Plans, called "Part C," combine Part A (hospital insurance) and Part B (medical insurance), and usually Part D (prescription drug plan). Private insurance companies approved by Medicare provide this coverage. Medicare Advantage Plans cover all Medicare services, and some plans also offer extra coverage, like vision, hearing, and dental coverage.

## Medicare Part D Prescription Drug Plan (PDP)

Medicare offers prescription drug coverage for everyone with Medicare. If a taxpayer decides not to join a PDP when first eligible, a late enrollment penalty may apply to all future Medicare prescription drug coverage premiums. The coverage is available through insurance companies approved by Medicare.

There are two ways to get coverage under a PDP. The participant may join a PDP that adds drug coverage to the original Medicare plan, or join a Medicare Advantage Plan that includes prescription drug coverage as part of the plan.

**How it works.** Under a PDP, a separate monthly premium applies. The individual makes copays or coinsurance payments, and a deductible applies. The individual receives a prescription card which is to be presented when prescriptions are filled. The individual must go to a pharmacy that belongs to the PDP network. Each PDP has a list of covered prescription drugs which may vary from plan to plan.

**Coverage gap ("donut hole").** Most Medicare drug plans have a coverage gap, also called the "donut hole." After the individual and the Medicare plan have spent \$5,030 (2024) for covered drugs, the individual must pay all costs out-of-pocket for prescriptions until the individual has paid enough out of pocket (\$8,000 for 2024) to qualify for catastrophic coverage.

For individuals who reach the coverage gap in 2024, a 75% discount applies on brand name or generic prescription drugs.

## Medigap (Medicare Supplemental Insurance)

A Medigap policy is health insurance sold by private insurance companies to fill gaps in the Medicare coverage. Medigap policies help pay the costs of Medicare-covered services (coinsurance, copayments, or deductibles), and some policies cover certain costs not covered by the Medicare Plan.

Insurance companies can sell only standardized Medigap policies that follow federal and state laws.

## Medicaid

Medicare and Medicaid are not the same program. Medicaid is a state-run program that provides hospital and medical coverage for people with low income and little or no resources. Each state has its own rules about who is eligible and what is covered. For more information, contact a local medical assistance agency, social services, or welfare office.