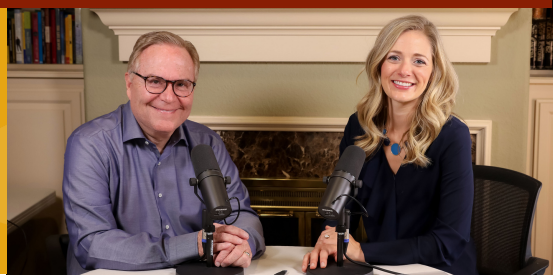
DEL MONTE GROUP

A Place of Possibility™

Episode 03 - Basics of Roth IRA

DMG's Know Your Possibilities Guide

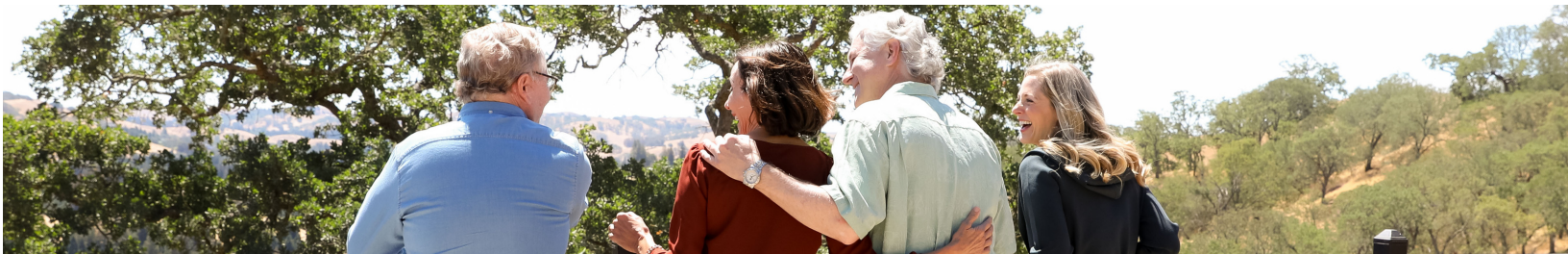
A Roth IRA is one of the best tools out there to build tax-free retirement income. So, why aren't more people taking advantage? Well, it is complex, and several rules scare people away. If you do have one, chances are you may not be maximizing the benefits. **You and your retirement deserve it all, so grab a pencil, press play, and let's discuss Roth IRAs.**



- **The Basics of a Roth IRA:**
  - Simply put, the main reason you would use a Roth IRA is so that you can get a tax-free income after age 59 ½.
  - You have to keep the money in the account for five years.
  - **Note:** The earnings are the only taxable part – if you pull it out before the five years are up or before your turn 59 ½.
  - What are the exceptions to that rule?
    - If you become permanently disabled.
    - You can take $10,000 out to purchase your first PRIMARY residence. AND, if you're a married couple, you each can take out $10,000. $20,000 for your first new home – yes, please!
    - You can also withdraw money if you are taking a series of substantially equal payments over a time period equalling the longer of five years or until you reach age 59.5.
    - Reimbursement for medical expenses up to 10% of your AGI.
    - Did you know you can take money out of your Roth without penalty if the IRS has levied you? Who knew!
    - If you're in the reserves, you can take qualified reservist distributions.
    - Natural disasters.
    - Or if you're taking it out for qualified education expenses. It's like a 529 – that's huge!
    - Covering the cost of childbirth or adoption.
- **Pro Tip:** your contributions can always come back out tax and penalty-free. So say you're maxing out your Roth, you can pull it all back out.
- **Pro Tip:** ALWAYS track your Roth contributions, so you know precisely what your basis is.

> ***"The IRS says the primary responsibility for monitoring your contributions is on you and your conversions. So, word to the wise."***

- **Why would you take money out of your Roth? Our recommendations:**
  - If you're young and you're purchasing your first new home – why not?
  - If you've made a mistake, you're in a jam with debt, and it's a one-time situation, you could certainly dip in to help, but don't forget to put it back!
  - Who can contribute to a Roth? It sounds pretty good so far, right?!
    - You've got to be working, have earned income whether you are employed or self-employed. Or, you must have a spouse who is working.
    - AKA: You must be paying social security tax on your income.
    - If you're a married couple, the "phase out" starts at $198,000, which means if you're making up to $198,000, you can contribute the full amount. If you earn over that, you can only contribute a portion of the full amount.



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  - If you earn over $208,000 as a married couple, you can't contribute – sorry.
  - Flying solo? The phase-out starts at $125,000, and if you make $140,000, no Roth for you.
- **What happens if you can't contribute – Let's discuss the workarounds!**
  - Instead of putting money into a Roth, you can't because of your income; you put it in a nondeductible IRA, and then as soon as the money hits, you convert it to a Roth. Tada!

> *"Limits, of course, there are limits to how much you can put in these things. So, it's $6,000. If you're under the age of 50, and $7,000 if you're over 50."*

  - But, yes, there is a but, you can't have any other IRA balances. Why? If you put the money in a nondeductible IRA, then do a Roth Conversion; they will take the basis of all your IRA accounts and then apply that tax to the amount you just converted in.
  - What if you want to do a conversion, but you already have a regular IRA hanging out? Backdoor alert! Move your IRA to some other type of retirement account. like your 401k at work, to get it off the books.
  - **NOTE:** If you're making regular monthly conversions, for example, every conversion has its own five-year period.
- **A Roth 401k – what?**
  - Some 401k plans have Roth-like provisions.
  - Instead of reducing your income by the amount you contribute to your 401k plan, there's no deduction at all, and all of the money comes back tax-free.
  - AND, 401k contribution limits are much higher - $19,500 if you're under 50 and $26,000 if you're over.
  - **SUPER Pro Tip:** Have you heard about the rule where you can put more money in – up to $38,000? If you add up the different sources of income that go into your 401k--your contributions, your employer's match, and then find the difference between that number and $58,000. That's how much extra you can contribute after-tax. And the cool thing? As soon as you put it in, you can convert it!
- **How do I maximize my contributions?**
  - Our recommendations: Swing for the fences (depending on your own personal risk tolerance) invest in allocations that give you the greatest return!
  - When do conversions make sense?
    - If you're a high earner and already paying a lot of taxes, this is not for you.
    - If you're in a lower tax bracket, this IS for you.
    - If you know your income will be lower – look at the situation and get strategic.
    - To avoid Medicare premiums going up due to higher income from retirement plan distributions, make sure you convert as early as possible.
- **Be warned! Don't fall for life insurance or retirement plan scams – they are NOT a replacement for a Roth!**

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Info@APlaceOfPossibility.com | 925.736.6410 |

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75 Golden Meadow Lane, Alamo, CA 94507
APlaceOfPossibility.com