



ED SLOTT'S IRA ADVISOR

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TAX & ESTATE PLANNING FOR YOUR RETIREMENT SAVINGS

Basis in an IRA

Basis in an IRA

It used to be that generally there was no “basis” in an IRA or any other retirement plan. Contributions were made with pre-tax dollars and earnings accumulated tax deferred. When a distribution was taken, the entire amount was taxed as ordinary income. Then, the tax laws changed and not all IRA contributions are deducted. Now, those who make nondeductible, after-tax contributions to their IRAs have basis (after-tax amounts) in their IRAs.

Then came the Roth IRA. This was a game changer when it comes to basis. Contributions to a Roth IRA are made with after-tax dollars which creates basis in the Roth IRA. The creation of the Roth IRA was followed by tax law changes allowing after-tax funds in employer plans to be rolled over to IRAs and the creation of Roth accounts in employer plans. In addition, we now have strategies such as the “back-door Roth IRA” and the “mega back-door Roth” that increase after-tax contributions to IRA and employer plan accounts. Consequently, we

The Roth IRA was a game changer when it comes to basis.

are seeing more basis or after-tax funds in retirement accounts than ever before.

What is Basis in an IRA?

Basis in most retirement accounts consists of after-tax dollars that have been contributed to that account. Basis can also come from after-tax funds that are moved from one retirement account to another, as in a rollover of basis from an employer plan to an IRA. Earnings on these basis amounts are tax deferred, *not* tax free. When earnings

are distributed, they are taxable as ordinary income. They can also be subject to the 10% early distribution penalty, if applicable. There is never a step-up in basis in any retirement account.

Roth IRAs are different. The earnings in a Roth IRA are tax free when the distribution is a qualified distribution. To be qualified, the distribution must be made more than five years after the *first* Roth account has been established **and** after age 59½, **or** due to death or disability, **or** the distribution is for a first-time

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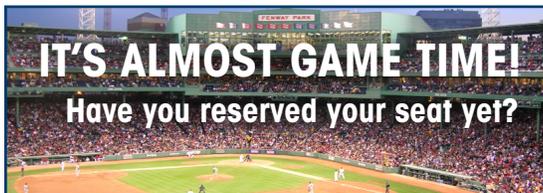
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Guest IRA Expert

David Buckwald, CFP®, CLU, ChFC, CLTC, NSSA
Atlas Advisory Group

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