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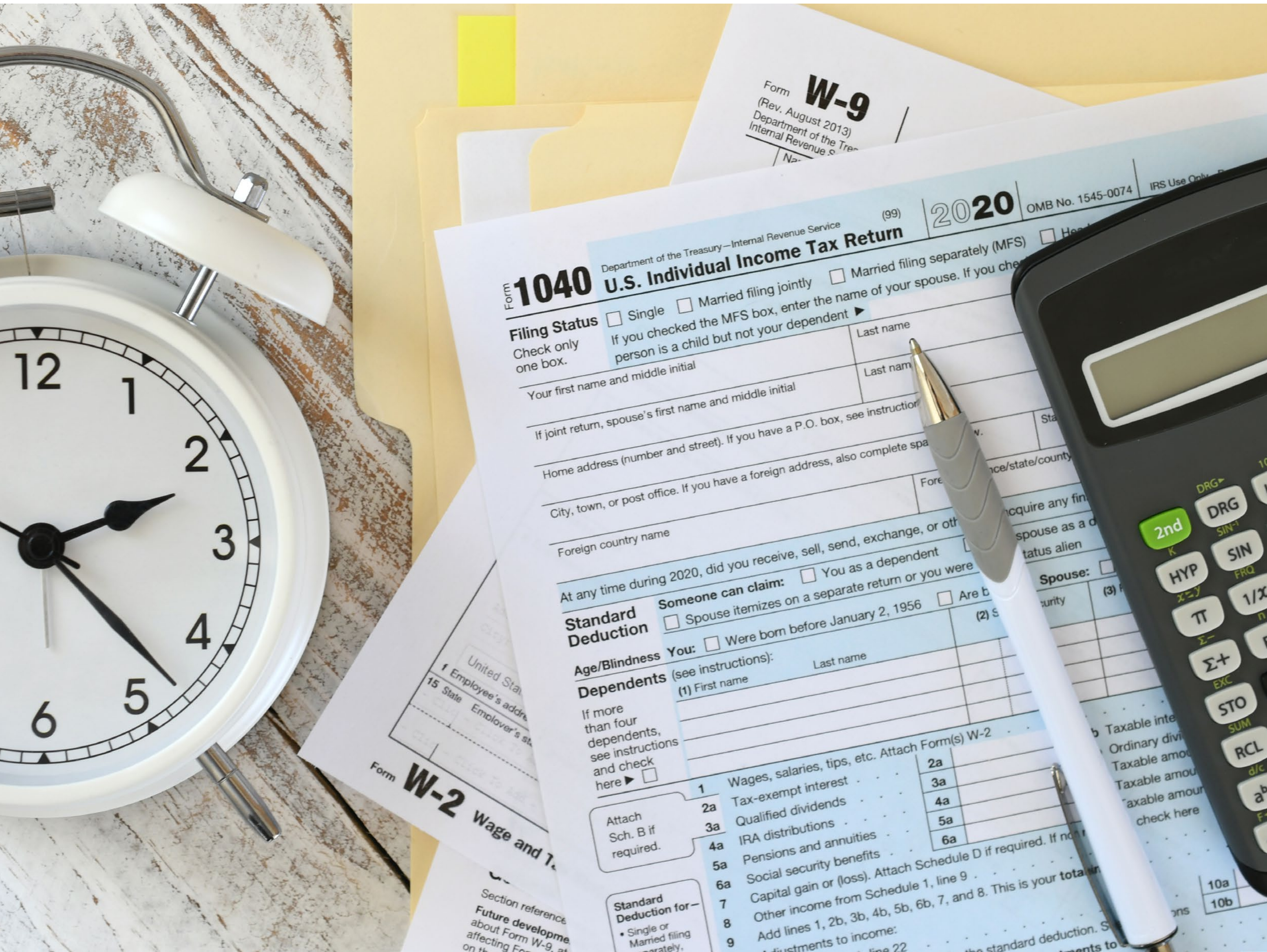

There is Still Time To Make an IRA Contribution for 2021

As you prepare your 2021 tax return, you may find yourself looking to reduce your taxes. A great way to reduce taxable income while saving for the future is by contributing to an Individual Retirement Account. Even though 2021 is over, you have until April 15, 2022, to contribute to an IRA for the 2021 tax year. This article will provide an overview of an IRA along with limits on contributions and tax deductibility.

Types of Individual Retirement Plans

There are two types of IRAs: a traditional IRA or a Roth IRA.

Traditional IRA

A traditional IRA is a tax-advantaged saving plan that you can open and fund yourself. You can contribute a portion of your annual income to the IRA subject to certain limitations. You receive an income tax deduction for contributions to the plan, thereby reducing your tax burden for the year in which the contributions are made. The IRA balance can grow tax-deferred, and then taxes are paid on future withdrawals.

Roth IRA

Like the traditional IRA, a Roth IRA is a retirement account that you can open and fund yourself. However, contributions to Roth IRAs are made after-tax, which means the contributions are not tax-deductible. The IRA balance grows tax-free, and withdrawals are made tax-free. A Roth IRA is often beneficial for individuals in a lower income tax bracket when they contribute funds to the IRA versus when they eventually withdraw funds.

Contribution Limitations

Each type of retirement plan has certain contribution limits and may be subject to income restrictions defined by the IRS.

The total amount that an individual may contribute to their traditional and Roth IRAs is $6,000 per year for those under age 50 and $7,000 per year for those 50 and older.

You cannot contribute more than your earned income for the year. For example, if you earned $4,000 in 2021, you cannot contribute more than $4,000 to your IRA.

If you don't have enough earned income to maximize your IRA contribution, but your spouse does, you might want to consider opening a spousal IRA. A Spousal IRA enables a spouse who individually does not meet the minimum income requirements, to contribute to an IRA based on the couple's combined income.

There are income limitations for contributing to a Roth IRA. You may not contribute to a Roth IRA if your modified adjusted gross income exceeds the following limits for 2021:

- $208,000 for married filing jointly or qualifying widow(er).
- $140,000 for single, head of household, or married filing separately (and you didn't live with your spouse at any time during the year)
- $10,000 for married filing separately (if you lived with your spouse at any time during the year)

If your income precludes you from contributing to a Roth IRA, you may consider making contributions to a nondeductible IRA and then convert it to a Roth IRA.

Tax Deduction Limitations

While there are no income limitations for contributing to a traditional IRA, there are certain limitations for how much of the contributions are tax-deductible.

If you are covered by another plan offered by an employer, then your 2021 modified adjusted gross income must be less than the following limits to receive a maximum deduction.

- $76,000 for single or head of household.
- $125,000 for married filing jointly or qualifying widow(er).
- $10,000 for married filing separately.

If you are not covered by another plan offered by an employer, then your 2021 modified adjusted gross income must be less than the following limits to receive a maximum deduction.

- No limit for single, head of household, qualifying widow(er),
- No limit married filing jointly or separately with a spouse who is not covered by an employer plan.
- $208,000 for married filing jointly with a spouse who is covered by an employer plan.
- $10,000 for married filing separately with a spouse who is covered by an employer plan.

Tax Excess IRA Contributions

Be careful not to contribute more than allowed to your IRA. Excess contributions are taxed at 6% per year for each year the excess amounts remain in the IRA.

Early Withdrawal Penalties

There is a 10% penalty for early withdrawals before age 59 and a half for both types of plans.

Final Thoughts

While this article provides a brief overview of traditional and Roth IRAs, it is not a substitute for speaking with one of our expert advisors. If you would like to discuss maximizing your tax savings, please contact our office.

About Hayashi Wayland

In 1976, Douglas Hayashi and Warren Wayland opened the doors to Hayashi Wayland. They based their partnership on the belief that a firm should measure its success by the success of its clients. They also believed that as a member of the community, the firm should work to strengthen it.

Today, Hayashi Wayland has grown to become the premier professional services firm on the Central Coast. We offer the greatest number of services of any firm in the area, from traditional accounting services to financial planning, and other consulting services.

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