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The Pension Digest

ALSO IN THIS ISSUE –

Collin W. Fritz and Associates, Inc.,
"The Pension Specialists"

IRA Contribution Limits for 2014 – Unchanged at $5,500 and $6,500

The 16-day government shutdown impacted the IRS. The IRS reopened on October 17. On October 31 the IRS released the 2014 IRA and pension limits.

Inflation was very low for the fiscal quarter ending September 30, 2013, so many of the IRA and pension limits as adjusted by the cost of living factor have not changed or the changes have been quite small.

The maximum IRA contribution limits for 2014 for traditional, Roth and SIMPLE IRAs did not change – $5,500/$6,500 and $12,000/$14,500 respectively.

The maximum contribution limit for SEP-IRAs is $52,000 for 2014 up from $51,000 for 2013.

The maximum limits for 401(k) participants for 2014 are also unchanged at $17,500/$23,000.

The IRA compensation limit changes were small, either $1,000 or $3,000.

Contribution limits for a person who is not age 50 or older.

Tax Year	Amount
2009	$5,000
2010	$5,000
2011	$5,000
2012	$5,000
2013	$5,500
2014	$5,500

Contribution Limits for a person who is age 50 or older.

Tax Year	Amount
2009	$6,000
2010	$6,000
2011	$6,000
2012	$6,000
2013	$6,500
2014	$6,500

IRS Issues 2014 IRA/Pension Limits

IRS Announces Cost-of-Living Adjustments for 2014
The IRS in News Release No. IR-2013-86 Released its 2014 Adjustments as Follows:

	2011	2012	2013	2014
Taxable Wage Base — OASDI Only	$106,800	$110,100	$113,700	$117,000
SEP and Qualified Plan Maximum Compensation Cap – 401(a)(17) & 404(e)	$245,000	$250,000	$255,000	$260,000
Elective (Salary) Deferral Limit – 401(k) & SAR-SEP	$16,500	$17,000	$17,500	$17,500
Elective Deferral Catch-up Limit	$5,500	$5,500	$5,500	$5,500
SIMPLE Deferral Limit – 408(p)(2)(A)	$11,500	$11,500	$12,000	$12,000
SIMPLE Catch-up Limit	$2,500	$2,500	$2,500	$2,500
Highly-Compensated Employees (Compensation as Indexed)	$110,000	$115,000	$115,000	$115,000
Defined Benefit Limit – Section 415(b)(1)(A)	$195,000	$200,000	$205,000	$210,000
Defined Contribution Limit – Section 415(c)(1)(A)	$49,000	$50,000	$51,000	$52,000
SEP Minimum Compensation Threshold – 408(k)(2)(c)	$550	$550	$550	$550
Key Employee Top Heavy — 41(i)(ii)(a)(i)	$160,000	$165,000	$165,000	$170,000

IRA Contribution Deductibility Chart for 2013

(for participants and/or spouses in employer-sponsored retirement plans.)

Amount of Modified AGI - (Combined modified AGI if married)

Single

Below $59,001	Entitled to full deduction
$59,001-$68,999.99	Entitled to prorated deduction amount - use special formula**
$69,000 or over	No deduction permissible

**Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $59,000/$10,000. This will give you a ratio that determines the amount you cannot deduct.*

Married - joint return, both are covered

Below $95,001	Entitled to full deduction
$95,001 - $114,999.99	Entitled to prorated deduction amount - use special formula**
$115,000 or Over	No deduction permissible

**Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $95,000/$20,000. This will give you a ratio that determines the amount you cannot deduct.*

Married - joint return, but only you are covered

Below $95,001	Fully Deductible
$95,001-$114,999.99	Entitled to prorated deduction amount - use special formula**
$115,000 or over	No deduction permissible

**Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $95,000/$20,000. This will give you a ratio that determines the amount you cannot deduct.*

Married - joint return, but only your spouse is covered

Below $178,001	Fully Deductible
$178,001-$187,999.99	Entitled to prorated deduction amount - use special formula**
$188,000 or over	No deduction permissible

**Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $178,000/$10,000. This will give you a ratio that determines the amount you cannot deduct.*

Married Filing Separately

Below $10,000	Entitled to prorated deduction amount - use special formula**
$10,000 or Over	No deduction permissible

**Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $0/$10,000. This will give you a ratio that determines the amount you cannot deduct.*

*Any amount determined under this formula which is not a multiple of $10 shall be rounded to the next lowest $10.

However, an IRA accountholder will be able to deduct a minimum of $200 as long as his or her AGI is not above the phase-out range (base amount plus $10,000).

IRA Contribution Deductibility Chart for 2014

(for participants and/or spouses in employer-sponsored retirement plans.)

Amount of Modified AGI - (Combined modified AGI if married)

Single

Below $60,001	Entitled to full deduction
$60,001-$69,999.99	Entitled to prorated deduction amount - use special formula**
$70,000 or over	No deduction permissible

**Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $60,000/$10,000. This will give you a ratio that determines the amount you cannot deduct.*

Married - joint return, both are covered

Below $96,001	Entitled to full deduction
$96,001 - $115,999.99	Entitled to prorated deduction amount - use special formula**
$116,000 or Over	No deduction permissible

**Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $96,000/$20,000. This will give you a ratio that determines the amount you cannot deduct.*

Married - joint return, but only you are covered

Below $96,001	Fully Deductible
$96,001-$115,999.99	Entitled to prorated deduction amount - use special formula**
$116,000 or over	No deduction permissible

**Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $96,000/$20,000. This will give you a ratio that determines the amount you cannot deduct.*

Married - joint return, but only your spouse is covered

Below $181,001	Fully Deductible
$181,001-$190,999.99	Entitled to prorated deduction amount - use special formula**
$191,000 or over	No deduction permissible

**Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $191,000/$10,000. This will give you a ratio that determines the amount you cannot deduct.*

Married Filing Separately

Below $10,000	Entitled to prorated deduction amount - use special formula**
$10,000 or Over	No deduction permissible

**Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $0/$10,000. This will give you a ratio that determines the amount you cannot deduct.*

*Any amount determined under this formula which is not a multiple of $10 shall be rounded to the next lowest $10.

However, an IRA accountholder will be able to deduct a minimum of $200 as long as his or her AGI is not above the phase-out range (base amount plus $10,000).

Roth IRA Contribution Chart for 2014

Amount of AGI and Filing Status

Single, Head of Household or Qualifying Widow(er)

Below $114,000	Entitled to full contribution amount
$114,000-$128,999.99	Entitled to prorated contribution amount–use special formula*
$129,000 or over	No contribution permissible

*Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $114,000/$15,000. This will give you a ratio that determines the amount you cannot contribute. Round to the lowest $10.00.

Married Filing Jointly

Below $181,000	Entitled to full contribution amount.
$181,000-190,999.99	Entitled to prorated contribution amount–use special formula.*
$191,000 or over	No contribution permissible.

*Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $181,000/$10,000. This will give you a ratio that determines the amount you cannot contribute. Round to the lowest $10.00.

Married Filing Separate Returns

$0-$9,999.99	Entitled to prorated contribution amount–use special formula*
$10,000 or Over	No contribution permissible

*Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $0/$10,000. This will give you a ratio that determines the amount you cannot contribute. Round to the lowest $10.00.

Roth IRA Contribution Chart for 2013

Amount of AGI and Filing Status

Single, Head of Household or Qualifying Widow(er)

Below $112,000	Entitled to full contribution amount
$112,000-$126,999.99	Entitled to prorated contribution amount–use special formula*
$127,000 or over	No contribution permissible

*Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $112,000/$15,000. This will give you a ratio that determines the amount you cannot contribute. Round to the lowest $10.00.

Married Filing Jointly

Below $178,000	Entitled to full contribution amount.
$178,000-187,999.99	Entitled to prorated contribution amount–use special formula.*
$188,000 or over	No contribution permissible.

*Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $178,000/$10,000. This will give you a ratio that determines the amount you cannot contribute. Round to the lowest $10.00.

Married Filing Separate Returns

$0-$9,999.99	Entitled to prorated contribution amount–use special formula*
$10,000 or Over	No contribution permissible

*Explanation of special formula. Multiply the permissible contribution by the following ratio: amount of adjusted gross income in excess of $0/$10,000. This will give you a ratio that determines the amount you cannot contribute. Round to the lowest $10.00.

SEP and SIMPLE Limits

	2011	2012	2013	2014
Maximum SEP Contribution	$49,000	$50,000	$51,000	$52,000
Maximum SIMPLE Deferral (Under age 50)	$11,500	$11,500	$12,000	$12,000
Maximum SIMPLE Deferral (Under Age 50 & older)	$14,000	$14,000	$14,500	$14,500

Saver's Credit Limits for 2014

The applicable percentage for 2014 is based on modified adjusted gross income (AGI) and your tax-filing status, and is determined by the following table:

Joint Return

AGI Over	AGI Not Over	Percentage
$0	$36,000	50%
$36,000	$39,000	20%
$39,000	$60,000	10%
$60,000	N/A	0%

Head of Household

AGI Over	AGI Not Over	Percentage
$0	$27,000	50%
$27,000	$29,250	20%
$29,250	$45,000	10%
$45,000	N/A	0%

Other Filers Including Married, Filing Separately

AGI Over	AGI Not Over	Percentage
$0	$18,000	50%
$18,000	$19,500	20%
$19,500	$30,000	10%
$30,000	N/A	0%

Saver's Credit Limits for 2013

The applicable percentage for 2013 is based on modified adjusted gross income (AGI) and your tax-filing status, and is determined by the following table:

Joint Return

AGI Over	AGI Not Over	Percentage
$0	$35,500	50%
$35,500	$38,500	20%
$38,500	$59,000	10%
$59,500	N/A	0%

Head of Household

AGI Over	AGI Not Over	Percentage
$0	$26,625	50%
$26,625	$28,875	20%
$28,875	$44,250	10%
$44,250	N/A	0%

Other Filers Including Married, Filing Separately

AGI Over	AGI Not Over	Percentage
$0	$17,750	50%
$17,750	$19,250	20%
$19,250	$29,500	10%
$29,500	N/A	0%

Customer HSA Tip – Paying Medical Insurance Premiums With HSA Funds Can Be Very Expensive

Almost everyone learns a tax lesson the hard way. One wishes to minimize such lessons.

Recently we had a consulting call because John Doe had come into the bank to open an HSA. His employer had established a high deductible health plan for all employees. He had informed his employees that they would be able to establish an HSA and then withdraw funds from their HSA on a tax-free basis if used to pay some or all of the monthly medical insurance premium.

The employer is wrong except for certain limited situations where the HSA owner's withdrawal of HSA funds to pay certain premiums will be tax free. See the following article discussing the exceptions.

The mistake can be very tax expensive. For example, John age 39, opens his HSA in January of 2013. His employer contributes $1,800 to his HSA and he contributes another $2,000. Every month he withdraws $280 to pay against the medical insurance premium. He withdraws a total of $3,360.

John visits his tax preparer in February of 2014. He is told he will need to pay income tax on the $3,360 since it was not used to pay a qualified medical expense. Assuming John is in the 15% tax bracket, he owes $504. He will owe another $672 since he owes the 20% pre-65 tax. The total is $1,176. Very expensive!

CWF is not aware of any authority which would allow the IRS to not seek collection of the $1,176 even if the employer would admit to the mistake. This is not a "mistaken distribution" as the IRS defines this term.

Basic Info to Acquire to Start Administration of an Inherited or Beneficiary IRA

Name of deceased
IRA accountholder ______________________________

DOB (date of birth) of IRA Accountholder___________

DOD (date of death) of IRA Accountholder _________

Name of
inheriting IRA Beneficiary ______________________

Beneficiary's Relationship ❍Spouse ❍Nonspouse

DOB (date of birth) of beneficiary ________________

Is an RMD required for year of death ❍Yes ❍No

Does the beneficiary need to take a
remaining RMD portion for such year? ❍Yes ❍No

Other steps

1. Determine beneficiary is CIP eligible.
2. Obtain copy of the death certificate or an equivalent.
3. Furnish the beneficiary with a copy of the form where he or she will instruct how and when distributions will be withdrawn. Be furnished a completed form. See CWF form 204.

   The form will provide the beneficiary's name, address and social security number.

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Rollover IRA Funds to 401(k) Plan to Lessen Upcoming RMDs from IRA

Certain individuals may wish to adopt the following planning technique.

Jane Doe is currently age 69 and she is still working for Roogle. She is a successful marketing executive, but she is not a 5% owner. Jane's date of birth is November 29, 1933. She will be age 70 on November 29, 2013 and she will be age 70½ on May 29, 2014.

Jane has a traditional IRA with First National Bank with a current balance of $265,000. In 2002 she had rolled over $175,000 from a prior employer's 401(k) plan. Set forth below is an estimate of her RMDs from her IRA for 2014-2016, totalling $29,882.

2014 $265,000/26.5 = $10,000

2015 $255,000/25.6 = $9,961

2016 $245,039/24.7 = $9,921

Total of Anticipated RMDs = $29,882

In 2009 she was hired by Roogle. She is a participant of the Roogle 401(k) plan and her current balance is $95,000. The Roogle 401(k) plan provides that a non-5% owner employee is required to take an RMD distribution for the year he or she separates from service and subsequent years. Prior to such year, any distribution is not a required distribution. However, if a person separates from service prior to age 70½, then he or she is required to commence RMDs for the year during the which he or she attains age 70½. Jane is planning to work for Roogle until January 2, 2017.

With respect to the Roogle 401(k) plan, Jane is not required to take a required distribution until the year she separates from service. This would be 2017. There would be no RMD for her for 2014, 2015, and 2016.

With respect to her IRA, Jane has a planning option if the Roogle 401(k) plan authorizes her to rollover her IRA funds into the 401(k) plan. In fact, the plan has been so written. She may roll over her IRA balance ($265,000) into the Roogle 401(k) plan. By doing this, she will not have to take an RMD with respect to the $265,000 for 2014-2016.

Should she do the rollover in 2013 or 2014?

She wants to do the rollover in 2013. By doing so, there will be no funds in her IRA as of December 31, 2013. This means she does not have to take a 2014 RMD from her IRA and there will be no RMD for 2015 and 2016.

What would be the situation if she would not do the rollover until January 20, 2014?

Jane has an IRA as of January 1, 2014. This means she has an RMD with respect to the traditional IRA of $10,000 for 2014. This amount is ineligible to be rolled over to the Roogle 401(k) plan or any plan or IRA. It does matter is she does the rollover prior to attaining age 70½. Because she attains age 70½ in 2014 and there is a balance in her IRA as of December 31, 2013, she will have an RMD for 2014.

Her rollover would be limited to $255,000 rather than the $265,000. She will avoid taking an RMD with respect to the remaining $255,000 until she separates from service.

An employee who is a 5% owner of the business sponsoring the 401(k) plan must take RMDs commencing with the year he or she attains age 70½ just as an IRA accountholder must.

When IRA funds are rolled over into a 401(k) plan such funds are no longer IRA funds. Such funds are not "rollover" funds within the 401(k) plan and all of the plan rules applying to distributions will apply to such funds. An individual who has the same situation as Jane De will most likely also want to rollover his or her IRA funds into the employer's 401(k) plan. Many individuals will have the attitude, "why take any distribution if one is not required?"

Please Note:

CWF's Consulting Hours
7:30a.m. - 4:20pm
Monday - Friday

Updated IRS – IRA Questions

The IRS has a number of tests for individuals who wish to serve as tax preparers. Set forth are nine IRA questions. The answers, with CWF's discussion, are provided following the test.

1. Which of the following statements is the best answer regarding contributions to traditional IRAs for 2013?

☐ a. The maximum amount taxpayers under age 50 may contribute to an IRA is $5,500.

☐ b. For married filing joint returns, the maximum IRA contribution cannot exceed $13,000 when both taxpayers are age 50 or older.

☐ c. The deadline for contributing to an IRA for the year 2013 is April 15, 2014.

☐ d. All of the above.

☐ e. None of the above.

2. Which of the following statements correctly describes the minimum distribution rules?

☐ a. Taxpayers are required to receive minimum distributions from qualified employee retirement plans, qualified annuity plans, deferred compensation plans, tax-sheltered annuity plans and traditional IRAs.

☐ b. A taxpayer is subject to an excise tax of 55% on required minimum distributions that are not taken.

☐ c. A taxpayer may avoid the excise tax on minimum distributions not taken by taking at least 90% of the required minimum distribution.

☐ d. All of the above.

☐ e. None of the above.

3. Alisha received a Form 1099-R for 2013. There is a "7" in box 7 or her form. What does the 7 stand for?

☐ a. Prohibited transaction

☐ b. Excess contribution

☐ c. Normal distribution

☐ d. Charitable gift annuity

4. Sam and Betty Lincoln retired in 2013. Sam has contributed to a traditional IRA for the last ten years, but he also participated in his employer's pension plan. He never deducted his IRA contributions. His IRA has averaged an earnings rate of 4.5% per year. Sam received a distribution from his IRA in the amount of $1,000 in 2013. Which of the following statements is true?

☐ a. The $1,000 distribution is taxable.

☐ b. The entire $1,000 distribution is not taxable.

☐ c. Sam must complete Form 8606 and attach it to his tax return.

☐ d. Form 1099-R will report the taxable portion of the IRA distribution.

5. Distributions from all IRAs are fully taxable with the exception of the Roth IRA.

☐ a. True

☐ b. False

6. Amy, age 60, contributed to a Roth IRA for 5 years. On year six, she became legally blind and took a distribution from her Roth IRA. The entire distribution is excluded from her taxable income.

☐ a. True

☐ b. False

7. Which transactions involving traditional IRAs are permitted without tax penalties?

☐ a. Taking distributions at age 57.

☐ b. Investing the IRA in art works and rare wines.

☐ c. Rolling over assets within 70 days.

☐ d. Rolling over assets within one year from the same IRA.

☐ e. None of the above.

IRA Test Answers

1. d. All of the above. Maximum contribution limit is $5,500 (under age 50) or $6,500 (age 50 or older) as of December 31, 2013.

2. a. The required distribution rules apply to traditional IRAs, pension plans and to a Roth IRA beneficiary.

3. c. A normal distribution means she was at least $59^1/_2$ when she received the distribution.

4. c. His IRA has both basis and earnings. The pro-rata distribution rule applies. A portion is taxable and a portion is not.

5. b. False. Not all distributions from all IRAs are fully taxable.

6. a. True. A qualified distribution occurs when the recipient of a Roth IRA distribution has met the 5-year rule and is age $59^1/_2$ or older.

7. e. A tax penalty would apply to the four listed transactions.

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Assisting When an Employer Customer Makes an HSA Depositing Error

A financial institution acting as an HSA custodian is a service provider. A service provider always wants to help a customer solve a problem as easily and simply as possible as long as the correcting action is authorized by law.

It will happen, an employer will make an HSA contribution, but there is an error relating to the contribution. For example. ABC School District instructs the HSA custodian to withdraw $12,400 from its checking account and then contribute the $12,400 to the HSAs of its 62 employees as instructed on a contribution sheet. The problem – the employer's contribution sheet as furnished to the HSA custodian showed a contribution for Jane Doe as being $300 when it only should have been $100 and the contribution amount for Mary Thomas was only $200 when it should have been $400. It was supposed to be $400 since Mary had asked the school if she could contribute $200 of her own funds in addition to what the school contributed. The school agreed to assist her in making a contribution of $200.

An employee of ABC School District may initially think he can call the HSA custodian, explain the errors and that the financial institution will correct the mistake by withdrawing $200 from Jane Doe's HSA and transferring it into Mary Thomas' HSA. Note that there are two mistakes and not just one. Both mistakes must be corrected separately.

The problem for all service providers is – sometimes the client may want to solve a problem using a correction technique not authorized by the law. This is beware time. A service provider does not want its client's problem to become its problem.

Federal tax law does not authorize the HSA custodian to correct the employer's error in the proposed simple manner. HSAs like IRAs are quasi-fiduciary accounts. The financial institution owns the assets on behalf of the HSA owner. The HSA custodian must report all contributions on the Form 5498-SA and all distributions on the Form 1099-SA. There is no IRS rule which says, a contribution or distribution becomes nonreportable when the employer makes an accounting or bookkeeping error.

An HSA custodian may choose to furnish this article to an employer. However, the employer must act on the advice of its accountant or attorney.

As with IRAs, the general rule is that once a contribution is made to a person's HSA, those funds are owned by the HSA owner. Even if the employer documents to the HSA custodian that an error has occurred or that errors have occurred, an HSA custodian does not have the legal right to withdraw from Jane Doe's HSA the excess contribution of $200 and either put the $200 into Mary Thomas's HSA or to return such $200 to the employer. See the following article for two exceptions.

Approach #1. The employer has two errors to correct. These errors may or may not be related. First, the employer must inform Mary Thomas of its mistake. It failed to contribute $200 for Mary Thomas and so it should make this contribution as soon as possible. Second, the employer should inform Jane Doe of its mistake (i.e. over-contributed $200 to her HSA) and that the mistake will be corrected by lowering the amount of future HSA contributions for her until the $200 is recovered. This approach is best when the excess is recovered before December 31.

Approach #2. Both the employer and the HSA custodian will obtain the written consent of the person to whom the "too large" contribution was made. In the above example, this would be Jane Doe. If the consent document would authorize it, the funds could be returned to the employer. Under this approach, Jane Doe would need to include the distribution in her income and pay the 20% penalty tax as it was not withdrawn and used to pay a qualified medical expense. The withdrawal in this situation is not the return of an excess contribution. It may be the employer would decide to compensate Jane Doe for her additional tax liability.

In summary, Approach #1 is the preferred correction method. The employer needs to correct its error by reducing its contributions for a certain employee or obtaining the employee's written consent that the mistaken contribution may be withdrawn from his or her HSA. The HSA custodian's role in the correction process is limited. The HSA will report all contributions on the Form 5498-SA and all distributions, if any, on the Form 1099-SA as normal HSA distributions.

Two Limited Exceptions for Mistaken Employer HSA Contribution

In July of 2008 the IRS issued Notice 2008-59. The IRS defined two limited exceptions allowing an employer to recoup its erroneous contributions.

The first exception – if it is determined an employee (or former employee) was never eligible for an HSA, then the employer is allowed to correct its contribution error by instructing the HSA custodian to return to the employer the nonqualifying contribution which had been made to the employee's HSA or former employee's HSA.

The second exception – if it is determined that an employer has made an HSA contribution to an employee's HSA or former employee's HSA which exceeds the current year's family contribution limit (either $6,450 and $7,450 for 2013 depending on the applicability of any catch-up contribution), then the employer is allowed to correct its contribution error by instructing the HSA custodian/trustee to return to the employer the nonqualifying or excess contribution amount.

There are no other exceptions allowing an employer to instruct the HSA custodian to pay it a certain amount so that it can recoup erroneous contributions from an employee's HSA or former employee's HSA.

Getting Rid of Basis Within a Traditional IRA so a Person can Convert Only the Non-Taxable Funds

There are individuals who have basis within one or more of their traditional IRAs. Remember that a person who has multiple traditional IRAs must aggregate all of them in applying the taxation rules when there is a distribution from one of more of the traditional IRAs.

Illustration. John Doe had $42,000 within his 401(k) plan; $32,000 was taxable (pre-tax) and the other $10,000 was nontaxable (after-tax or basis). He had directly rolled over the $42,000 into his traditional IRA in 2011. He had not used the planning technique as discussed in the article, "Moving Nondeductible Funds From a 401(k) Plan into a Roth IRA" as set forth in the July newsletter. Since 2011, there has been $8,000 of earnings within the traditional IRA. The IRA balance is now $50,000 and $10,000 is basis.

On page 5 is discussed the topic that a person is subject to the RMD rules may reduce his or her required distributions for a number or upcoming years by rolling over traditional IRA funds into a 401(k) plan.

This article is being written to illustrate that a person who has basis within his or her traditional IRA can isolate this basis by rolling over the "taxable" traditional IRA funds into a 401(k) plan or other pension plan. The individual may then convert this basis to a Roth IRA. Every taxpayer who is able to do this will want to do this. A two/three step process must be followed.

Step One. He rolls over or directly rolls over $40,000 from his IRA to the 401(k) plan. The rollover rules do not allow him to rollover the $10,000 of nontaxable funds within the traditional IRA to the 401(k) plan.

Step Two. He may now convert the $10,000 to his Roth IRA. No income tax is owed and the $10,000 in the Roth IRA will now be invested so that tax-free income will be earned. As long as there is a qualified distribution , it will be tax free.

Now that John has no taxable money within his traditional IRA, he most likely also will want to make a nondeductible traditional IRA contribution of $5,500 or $6,500 and convert such amount.

Step Three. This step is optional. After a short period of having these funds within the 401(k) plan back into the same or another traditional IRA as long as the 401(k) plan would permit it.

The key element of these planning techniques is, he must be eligible to make a rollover contribution into a 401(k) plan or another pension plan. If an individual does not have an employer who sponsors a 401(k) or other pension plan allowing such rollovers, but he has self-employment income from a business activity, he may set up his own 401(k) or pension plan so that such rollover may be made.