**Chapter 13. Retirement Plans. Assume the tax year is 2017, unless the question specifies another year.**

**Part I. 1. Page 13-3. Describe the tax and nontax aspects of employer-provided defined benefit plans from both the employer’s and employee's perspective.**

 Which of these statements is true regarding employer-provided qualified retirement plans?

|  |  |  |
| --- | --- | --- |
| **a.** | May discriminate against rank and file employees. | **D** |
| **b.** | Deductible contributions are generally phased-out based on AGI. |
| **c.** | Executives are generally ineligible to participate in these plans. |
| **d.** | They are generally referred to as defined benefit plans or defined contribution plans. |

**See discussion in text.**

 Which statement describes a defined benefit plan?

|  |  |  |
| --- | --- | --- |
| **a.** | Provides fixed income to the plan participants based on a formula | **A** |
| **b.** | Distribution amounts determined by employee and employer contributions |
| **c.** | Allows executives to defer income for a period of years |
| **d.** | Retirement account set up by an individual |

**Defined benefit plans pay a fixed income or benefit to the employee. This amount is
usually based on the average income of the employee and the years of service.
These plans are set up and funded by employers for employees.**

 Which of these statements regarding defined benefit plans is false?

|  |  |  |
| --- | --- | --- |
| **a.** | The benefits are based on a fixed formula | **C** |
| **b.** | The vesting period can be based on a graded or cliff schedule |
| **c.** | Employees bear the investment risks of the plan |
| **d.** | Employers are generally required to make annual contributions to meet expected future liabilities |

**Employees do not bear the risk of the plan's investment.**

 Which of these statements regarding vesting in a defined benefit plan is correct?

|  |  |  |
| --- | --- | --- |
| **a.** | Under a cliff vesting schedule, a portion of an employee's benefits vest each year. | **D** |
| **b.** | Under a graded vesting schedule, an employee's entire benefit vests all at the same time. |
| **c.** | When an employee's benefits vest, she is entitled to participate in the employer's defined benefit plan. |
| **d.** | When an employee's benefits vest, she is legally entitled to receive the benefits. |

**To vest in a benefit means to be legally entitled to receive it.**

Which of the following best describes distributions from a defined benefit plan?

|  |  |  |
| --- | --- | --- |
| **a.** | Distributions from defined benefit plans are fully taxable as ordinary income. | **A** |
| **b.** | Distributions from defined benefit plans are partially taxable as ordinary income and partially nontaxable as a return of capital. |
| **c.** | Distributions from defined benefit plans are fully taxable as capital gains. |
| **d.** | Distributions from defined benefit plans are partially taxable as capital gains and partially nontaxable as a return of capital. |

**The full amount of distributions from defined benefit plans is taxable as ordinary income.**

**2. Page 13-5. Explain and determine tax consequences of employer-provided defined contribution plans, including traditional 401(k) & Roth 401(k) plans.**

Which of the following describes a defined contribution plan?

|  |  |  |
| --- | --- | --- |
| **a.** | Provides guaranteed income on retirement to plan participants. | **B** |
| **b.** | Employers and employees generally may contribute to the plan. |
| **c.** | The plans are generally set up to defer income for executives and highly compensated employees but not for other employees. |
| **d.** | Retirement account set up to provide an individual a fixed amount of income on retirement. |

**Employers and employees generally contribute to the plan.**

Shauna received a distribution from her 401(k) account this year.
In which of the following situations will Shauna be subject to an early distribution penalty?

|  |  |  |
| --- | --- | --- |
| **a.** | Shauna is 60 years of age but not yet retired when she receives the distribution. | **B** |
| **b.** | Shauna is 58 years of age but not yet retired when she receives the distribution. |
| **c.** | Shauna is 58 years of age and retired when she receives the distribution. |
| **d.** | Shauna is 69 years of age but not yet retired when she receives the distribution. |

**Taxpayers are subject to an early distribution penalty if they receive a distribution before
they reach 59 ½ and are not retired, or have retired but not reached 55 years of age.**

Shauna received a $100,000 distribution from her 401(k) account this year.
Shauna's marginal tax rate is 25%. She has not yet retired.

Shauna received the distribution on her 59th birthday.

What is the total amount of tax and penalty Shauna will be required to pay?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $0.  | **b.** | $10,000.  | **c.** | $25,000.  | **d.**  | $35,000. | **e.** | Other | **D** |

**She must pay $25,000 of income tax on the distribution and a 10% early distribution penalty
because she was not 59 ½ on the date of the distribution and she had not yet retired.**

Riley participates in his employer's 401(k) plan. He retired in 2017 at age 75.
When must Riley receive his first distribution, in order to avoid minimum distribution penalties?

|  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | April 1, 2017  | **b.** | April 1, 2018 | **c.** | December 31, 2017  | **d.**  | December 31, 2018 | **B** |

**To avoid minimum distribution penalties, the taxpayer must receive the first distribution by no later than April 1 of the year after which the employee turns 70 ½ or the year in which the employee retires (if later). Because Riley is over 70 ½ years of age and he has retired he can receive his distribution no later than April 1 of 2018.**

 Pam is an employee of Geiger Technology and earns $90,000 in 2017.
The maximum amount Geiger can contribute to a profit sharing plan on behalf of Pam is:

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $ 6,000 | **b.** | $13,500 | **c.** | $22,500 | **d.**  | $25,000 | **e.** | $45,000 | **C** |

 Jenny (age 35) is considering making a one-time contribution to either a traditional 401(k) plan

or to a Roth 401(k) plan. She plans to withdraw the account balance when she retires in 40 years.

Jenny expects to earn a 7% before-tax rate of return no matter which plan she contributes to.
Which of the following statements is true?

|  |  |  |
| --- | --- | --- |
| **a.** | If Jenny's marginal tax rate in the year of contribution is higher than her marginal tax  | **A** |
|  | rate in the year of distribution, she will earn a higher after-tax rate of return on the  |
|  | traditional 401(k) plan than on the Roth 401(k) plan. |
| **b.** | If Jenny's marginal tax rate in the year of contribution is lower than her marginal tax rate in the year of distribution, she will earn a higher after-tax rate of return on the traditional 401(k) plan than on the Roth 401(k) plan. |
| **c.** | Jenny will earn the same after-tax rate of return no matter which plan she contributes to. |
| **d.** | Jenny is not allowed to make a one-time contribution to either plan. |

**If her marginal tax rate is higher in the year of contribution than in the year of distribution,**

**her after-tax rate of return will be higher for a traditional 401(k) plan because she will be**

**getting the tax benefit of the deduction at a higher rate and will have to pay the tax cost**

**of the distribution at a lower rate.**

 Heidi has contributed $20,000 in total to her Roth 401(k) account over a six-year period.
In 2017, her account was worth $50,000. Heidi was in desperate need of cash.

Heidi received a $30,000 nonqualified distribution from the account in 2017.
How much of the distribution will be subject to income tax and 10% penalty?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $0  | **b.** | $10,000  | **c.** | $12,000  | **d.**  | $18,000  | **e.** | $30,000 | **D** |

**Heidi is not taxed on 40% of the distribution because this is considered a return of her
nondeductible contribution. The 40% is the amount of her contributions divided by the value
of the account ($20,000/$50,000). The remaining 60% ($18,000) is subject to tax and penalties.**

Compare the rules for early distributions from Roth 401(k) and non-qualified distributions from Roth IRAs.

**3. Page 13-14. Tax implications of deferred compensation from employer's & employee's perspective.**

Which of these statements is true concerning employer funding of
nonqualified deferred compensation plans?

|  |  |  |
| --- | --- | --- |
| **a.** | Employers are required to invest salary deferred by employees in investments  | **D** |
|  | specified by the employees. |
| **b.** | Employers are required to annually fund deferred compensation obligations to employees. |
| **c.** | Employers annually deduct the amount earned by employees under the plan. |
| **d.** | Employers may discriminate in terms of who they allow to participate in the plan. |

**See discussion of nonqualified deferred compensation plans in the text.**

Which of these statements concerning nonqualified deferred compensation plans is true?

|  |  |  |
| --- | --- | --- |
| **a.** | If an employer doesn't have the funds to pay the employee, the employee becomes an  | **A** |
|  | unsecured creditor of the employer. |
| **b.** | These plans can be an important tax planning tool for employers if they expect their marginal tax rate to decrease over time. |
| **c.** | These plans can be an important tax planning tool for employees who expect their marginal tax rate to increase over time. |
| **d.** | Distributions are taxed at the same tax rate as long-term capital gains. |

**See discussion on nonqualified deferred compensation plans in text.**

 Which of the following statements comparing qualified defined contribution plans
and nonqualified deferred compensation plans is false?

|  |  |  |
| --- | --- | --- |
| **a.** | Employers must fund qualified defined contribution plans but not  | **D** |
|  | nonqualified deferred compensation plans. |
| **b.** | Qualified defined contribution plans are subject to formal vesting requirements while nonqualified deferred compensation plans are not. |
| **c.** | Distributions from both types of plans are taxed at ordinary income tax rates. |
| **d.** | In terms of tax consequences to the employee, earnings on qualified plans (except Roth plans) are deferred until distributed to the employee but earnings on nonqualified plans are immediately taxable. |

**Employees are not taxed on nonqualified deferred compensation plans until they receive distributions from the plans.**

**6. Page 13-30. Compute the saver's credit.**

 Which of the following taxpayers is most likely to qualify for the saver's credit?

|  |  |  |
| --- | --- | --- |
| **a.** | A low AGI taxpayer who does not contribute to any qualified retirement plan. | **B** |
| **b.** | A low AGI taxpayer who contributes to her employer's 401(k) plan. |
| **c.** | A high AGI self-employed taxpayer. |
| **d.** | A high AGI employee who does not contribute to any qualified retirement plan. |

**To be eligible for the saver's credit a taxpayer must contribute to a qualified retirement**

**plan (including IRAs). Further, the credit is phased out completely for high AGI taxpayers.**

 Amy is single and a part-time college student. In 2017, her adjusted gross
income was $12,000. During the year, Amy also contributed $2,500 to a Roth IRA.

What is the maximum saver's credit she may claim for the year?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $1,250  | **b.** | $2,500  | **c.** | $1,000  | **d.**  | $0 | **e.** | Other | **C** |

**$2,000 x 50% (the maximum contribution eligible for the credit multiplied
by the maximum applicable percentage based on filing status and AGI).**

 Amy is single and a part-time college student. In 2017, her AGI was $12,000.
During the year, Amy contributed $1,500 to a Roth IRA.
What is the maximum saver's credit she may claim for the year?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $750  | **b.** | $1,000  | **c.** | $1,500  | **d.**  | $0 | **e.** |  | **A** |

**$1,500 x 50% (her IRA contribution multiplied by the maximum applicable percentage
based on filing status and AGI).**

 Amy files as a head of household. Her AGI in 2017 was $60,000.
During the year, she contributed $2,500 to a Roth IRA.
What is the maximum saver's credit she may claim for 2017?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $1,000  | **b.** | $2,000  | **c.** | $2,500  | **d.**  | $1,250  | **e.** | $0 | **E** |

**Her AGI is too high to claim any saver's credit. Upper AGI limit is $46,500, inflation adjusted.**

 What is the maximum saver's credit available to any taxpayer in 2017?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $2,000  | **b.** | $1,000  | **c.** | $500 |  |  |  |  | **B** |

**The maximum saver's credit is $1,000 which is 50% of $2,000. While higher AGIs**

**affect the credit percentage, the maximum is $1,000 no matter the taxpayer's filing status.**

**Chapter 13. Retirement Planning- Part II**

**4. Page 13-19. IRAs Determine the tax consequences of traditional and Roth Individual Retirement Accounts and explain the differences between them.**

 Which of these statements regarding traditional IRAs is true?

|  |  |  |
| --- | --- | --- |
| **a.** | A taxpayer over the age 55 years of age is allowed to contribute an additional $1,000 a year. | **D** |
| **b.** | Taxpayers with high income are not allowed to contribute to traditional IRAs. |
| **c.** | Taxpayers who participate in an employer-sponsored retirement plan are allowed to contribute to a traditional IRA regardless of their AGI. |
| **d.** | A single taxpayer with no earned income is NOT allowed to deduct contributions to traditional IRAs. |

 Which of these statements regarding IRAs is false?

|  |  |  |
| --- | --- | --- |
| **a.** | Taxpayers who participate in an employer-sponsored retirement plan may be  | **D** |
|  |  allowed to make deductible contributions to a traditional IRA. |  |
| **b.** | The ability to make deductible contributions to a traditional IRA and nondeductible contributions to a Roth IRA may be subject to phase-out based on AGI. |
| **c.** | A taxpayer may contribute to a traditional IRA in 2017 but deduct the contribution in 2016. |
| **d.** | Taxpayers who have made nondeductible contributions to a traditional IRA are taxed on the full proceeds when they receive distributions from the IRA. |

 [Sec. 72(t)] Bryan (45 years old) had some unexpected medical expenses in 2017. To pay for
these expenses (which were claimed as itemized deductions on his tax return), he received a $20,000 distribution from his traditional IRA. He has only made deductible contributions to the IRA. His marginal ordinary income tax rate is 15%.

What amount of taxes and/or early distribution penalties will Bryan pay on this distribution?

|  |  |  |
| --- | --- | --- |
| **a.** | $3,000 income tax; $2,000 early distribution penalty | **B** |
| **b.** | $3,000 income tax; $0 early distribution penalty |
| **c.** | $0 income tax; $2,000 early distribution penalty |
| **d.** | $0 income tax; $0 early distribution penalty |

 Which of these statements regarding Roth IRAs is false?

|  |  |  |
| --- | --- | --- |
| **a.** | Contributions to Roth IRAs are not deductible. | **D** |
| **b.** | Qualifying distributions from Roth IRAs are not taxable. |
| **c.** | Whether or not they participate in an employer-sponsored retirement plan, taxpayers are allowed to contribute to Roth IRAs as long as their AGI does not exceed certain thresholds. |
| **d.** | Taxpayers who are married and file separately are not allowed to contribute to a Roth IRA. |

Which of these statements concerning traditional IRAs and Roth IRAs is true?

|  |  |  |
| --- | --- | --- |
| **a.** | A taxpayer may contribute to a Roth IRA at any age but a taxpayer is not allowed to  | **D** |
|  | contribute to a traditional IRA after reaching 70 ½ years of age. |  |
| **b.** | The annual contribution limits for a traditional IRA and Roth IRA are the same. |
| **c.** | Taxpayers with high income are allowed to contribute to traditional IRAs but not to Roth IRAs. |
| **d.** | All of the above are true statements. |

 In 2017 Jacob, a 19-year-old full-time student, earned $4,500 during the year and
was not eligible to participate in an employer-sponsored retirement plan.
The general limit for deductible contributions in 2017 is $5,500.
How much of a tax-deductible contribution can Jacob make to an IRA?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $0 | **b.** | $500 | **c.** | $4,500 | **d.**  | $5,000 |  |  | **C** |

Dan is single and is not covered by a company sponsored retirement plan.

His salary was $200,000 for the year**.** He is 45 years old.

What is his maximum deduction for a contribution to the IRA for **2017**?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $0 | **b.** | $5,500. | **c.** | $7,500 | **d.**  | $10,000 | **e.** | Other | **B** |

David is single and is covered by a company sponsored retirement plan.
His salary was $50,000 for the year**.** He is 45 years old.

What is his maximum deduction for a contribution to the IRA for **2017**?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $0 | **b.** | $5,500. | **c.** | $7,500 | **d.**  | $10,000 | **e.** | Other | **B** |

**Adjusted gross income is not over $62,000.**

Dawn is single and is covered by a company sponsored retirement plan.
Her salary was $65,000 for 2017**.** She is 45 years old.

What is her maximum deduction for a contribution to the IRA for **2017**?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $1,500 | **b.** | $2,000 | **c.** | $3,850. | **d.**  | $5,500 | **e.** | $10,000 | **C** |

**See Excel spreadsheet with answers.**

Bill and Betty are 33 years of age, married and file a joint return.

Each earns a salary of $40,000. Total is $80,000.

Both are covered by a retirement plan at work.

Each contributes $5,500 to an IRA (Total $11,000).

What is their total deduction for contributions to the IRA’s on a joint return for **2017**?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $0 | **b.** | $5,000. | **c.** | $7,500 | **d.**  | $11,000 | **e.** | Other | **D** |

Ben and Barbara are 33 years of age, married and file a joint return.

Each earns a salary of $56,500. Total is $113,000.

They are both covered by a retirement plan at work.

They each contribute $5,000 to an IRA (Total $10,000).
What is their total deduction for contributions to the IRA’s on a joint return for **2017**?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $3,300 | **b.** | $5,000. | **c.** | $7,500 | **d.**  | $10,000 | **e.** | Other | **A** |

 Ross and Rebba are both in their 30's. They are married and file a joint return.

Rebba earns $64,000 annually, and Ross earns $1,800 annually working part time.

Their adjusted gross income is $79,500.

Rebba participates in an employer-sponsored retirement plan, but Ross does not.

Rebba and Ross contribute the maximum amount allowable annually to their IRAs.

 What is their allowable deduction for their IRA contributions in 2017?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $ - 0 - | **b.** | $ 1,800 | **c.** | $ 5,000 | **d.**  | $ 6,800 | **e.** | $11,000 | **E** |

Jan and Joe (both age 30) are married and file a joint return.
Each earns a salary of $97,500. (Total is $195,000.)
Both Jan and Joe are active participants in their company's qualified pension plan.

They have never established an Individual Retirement Account, before the current year.
What is the maximum combined amount they can contribute to **Roth IRAs** for **2017**?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $ - 0 - | **b.** | $ 2,000 | **c.** | $ 5,000 | **d.** | $ 1,100 | **e.** | $10,000 | **D** |

What type of IRA is preferred when an individual expects to be in an income tax bracket
in retirement years that is lower than the tax bracket during the individual’s working years?

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | Regular IRA | **b.** | Roth IRA | **c.**  | Either |  | A |

**IRA Distributions, penalties**

 Kim who is age 40, took a distribution of $40,000 from her IRA in 2017 to buy
a sports car. Kim is subject to a penalty of:

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $4,000 | **b.** | $2,500 | **c.** | $1,000 | **d.**  | $ 500 | **e.** | $ -0- | **A** |

**She pays regular income tax on the distribution, and the 10% early distribution penalty as well.**

 Which of the following statements regarding Roth IRA’s distributions is true?

|  |  |  |
| --- | --- | --- |
| **a.** | A distribution is not a qualifying distribution unless the distribution is at least  | **C** |
|  |  two years after the taxpayer has opened the Roth IRA. |  |
| **b.** | A taxpayer receiving a distribution from a Roth IRA before reaching the age of 55 is generally not subject to an early distribution penalty. |
| **c.** | A Roth IRA does not have minimum distribution requirements. |
| **d.** | The full amount of all non-qualifying distributions is subject to tax at the taxpayer's marginal tax rate. |

 Daniela retired at the age of 65. The current balance in her Roth IRA is $200,000. Daniela established the Roth IRA 10 years ago. Through a rollover and annual contributions Daniela has contributed $80,000 to her account. Daniela received a $50,000 distribution from the Roth IRA. What amount of the distribution is taxable?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $0  | **b.** | $20,000  | **c.** | $30,000  | **d.**  | $50,000 |  |  | **A** |

 In 2017, Lisa, age 45, needed some cash so she received a $50,000 distribution from her Roth IRA. At the time of the distribution, the balance in the Roth IRA was $200,000.
Lisa established the Roth IRA 8 years ago.
Through a rollover and annual contributions, she has contributed $80,000 to her account.
What amount of the distribution is taxable and subject to early distribution penalty?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $0  | **b.** | $20,000  | **c.** | $30,000  | **d.**  | $50,000 |  |  | **A** |

**Her “nonqualified” distribution (before age 59.5) did not exceed her contributions to the plan.**

In 2017, Lisa, age 45, needed some cash so she received a $50,000 distribution from her Roth IRA. At the time of the distribution, the balance in the Roth IRA was $200,000.
Lisa established the Roth IRA 10 years ago.
Over the years, she has contributed $20,000 to her account.
What amount of the distribution is taxable and subject to early distribution penalty?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $0  | **b.** | $5,000  | **c.** | $30,000  | **d.**  | $50,000 |  |  | **C** |

**Her “nonqualified” distribution (before age 59.5) exceeded her contributions to the plan.**

Tyson (48 years old) owns a traditional IRA with a current balance of $50,000.
The balance consists of $30,000 of deductible contributions and $20,000 of account earnings.
Tyson believes that his marginal tax rate will increase in the future.
Tyson receives a distribution of the entire $50,000 balance of his traditional IRA.

He immediately contributes the $50,000 to a Roth IRA. His marginal tax rate is 25%.

What amount of penalty, if any, must Tyson pay on the distribution from the traditional IRA?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $0.  | **b.** | $1,250.  | **c.** | $3,750.  | **d.**  | $5,000. |  |  | **A** |

Tyson (48 years old) owns a traditional IRA with a current balance of $50,000.
The balance consists of $30,000 of deductible contributions and $20,000 of account earnings.
Tyson’s marginal rate is 25%. Tyson believes that his marginal tax rate will increase in the future.
Tyson receives a distribution of the entire $50,000 balance of his traditional IRA.

He retains $12,500 to pay tax on the distribution and he contributes $37,500 to a Roth IRA.
What amount of income tax and penalty must Tyson pay on this series of transactions?

|  |  |  |
| --- | --- | --- |
| **a.** | $0 income tax; $0 penalty. | **B** |
| **b.** | $12,500 income tax; $1,250 penalty. |
| **c.** | $12,500 income tax; $3,000 penalty. |
| **d.** | $12,500 income tax; $5,000 penalty. |
| **e.** | $0 income tax; $5,000 penalty. |

 In 2017, Jessica retired at the age of 65. The current balance in her traditional IRA was $200,000. Over the years, Jessica has made $20,000 of nondeductible contributions.

She also made $60,000 of deductible contributions to the account.
Jessica receives a $50,000 distribution from the IRA.

What amount of the distribution is included in income?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $0  | **b.** | $5,000  | **c.** | $37,500  | **d.**  | $45,000  | **e.** | $50,000 | **D** |

 Bob is 60 years of age in 2017. He opened a Roth IRA in 2013, and contributed $5,000 per year to the Roth IRA on January 2 of each of these four years: 2013, 2014, 2015 and 2016 (total $20,000). In 2017, the balance (including earnings) is $24,000. In 2017, Bob withdraws $20,000 from the Roth IRA and uses the funds to purchase a new auto.
What amount of the distribution is included in income for 2017?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $2,000  | **b.** | $5,000  | **c.** | $0  | **d.**  | $45,000  | **e.** | $50,000 | **C** |

 Betty is 60 years of age in 2017. She opened a Roth IRA in 2013, and contributed $5,000 per year to the Roth IRA on January 2 of each of these four years: 2013, 2014, 2015 and 2016 (total $20,000). In 2017, the balance (including earnings) is $24,000.
In 2017, Betty withdraws $22,000 from the Roth IRA and uses the funds to purchase a new auto.
What amount of the distribution is included in income for 2017?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $2,000  | **b.** | $5,000  | **c.** | $20,000  | **d.**  | $45,000  | **e.** | Other | **A** |

 Betty is 60 years of age in 2017. She opened a Roth IRA in 2013, and contributed $5,000 per year to the Roth IRA on January 2 of each of these four years: 2013, 2014, 2015 and 2016 (total $20,000). In 2017, the balance (including earnings) is $24,000.
In 2017, Betty withdraws $22,000 from the Roth IRA and uses the funds to purchase a new auto.
How much is the penalty associated with this withdrawal?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $200  | **b.** | $2,000  | **c.** | $20,000  | **d.**  | 0  | **e.** | Other | **A** |

**Retirement Savings- Part III.**

**5. Page 13-27. Describe retirement savings options available to self-employed taxpayers and compute the limits for deductible contributions to retirement accounts for self-employed taxpayers.**

Mary is a MACC graduate with her own unincorporated CPA firm.
She has two employees, paying one $50,000 per year, and the other $30,000 per year.
Her income statement for 2016 is as follows.

|  |  |
| --- | --- |
| Professional fees | $300,000 |
| Salaries | $80,000 |
| Rent and other operating expenses | $75,000 |
| Net income before pension contributions and S.E tax. | $145,000 |

Assume she has a Simplified Employee Pension plan. She makes the maximum contribution.

What is the total amount that should she contribute to IRAs owned by employees?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $0  | **b.** | $20,000  | **c.** | $25,000  | **d.**  | $8,000 |  |  | **B** |

**See Excel Answers.**

Repeat the preceding question. Assume that total salaries for all employees
amounted to $100,000. This changes $145,000 above to $125,000.
Mary contributed a total of $25,000 to the IRAs of employees.
What is her maximum contribution to her own SEP-IRA?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $0  | **b.** | $8,000 | **c.** | $25,235  | **d.**  | $18,587  |  |  | **D** |

**See Excel Answers. Also page 13-27 in textbook.**

 Which of the following is not a self-employed retirement account?

|  |  |  |
| --- | --- | --- |
| **a.** | SEP IRA | **B** |
| **b.** | SEM 403(c) |
| **c.** | Individual 401k |
| **d.** | None of the above. All of the above are self-employed retirement accounts. |

**See discussion in text.**

  In general, which of these statements regarding self-employed retirement accounts is true?

|  |  |  |
| --- | --- | --- |
| **a.** | SEP IRAs have higher contribution limits than individual 401(k)s if the  | **C** |
|  | contributing taxpayer is at least 50 years of age at year end. |  |
| **b.** | SEP IRAs have higher contribution limits than individual 401(k)s no matter the age of the contributing taxpayer. |
| **c.** | Individual 401(k)s have higher contribution limits than SEP IRAs. |
| **d.** | None of the above. Both SEP IRAs and individual 401(k)s have exactly the same annual contribution limits. |

**See discussion in the text. See page 13-29 vs. 13-28.**

Which of these statements regarding self-employed retirement accounts is true?

|  |  |  |
| --- | --- | --- |
| **a.** | A self-employed taxpayer who has hired employees may not set up a SEP IRA. | **C** |
| **b.** | A self-employed taxpayer who has hired employees may set up either a SEP IRA or an individual 401(k). |
| **c.** | A self-employed taxpayer who has hired employees may not set up an individual 401(k). |
| **d.** | All of the above statements are false. |

**See discussion of nontax factors of self-employed retirement accounts in text.**

Which of the following is true concerning SEP IRAs?

|  |  |  |
| --- | --- | --- |
| **a.** | SEP IRAs are difficult to set up and have high administrative costs | **D** |
| **b.** | Taxpayers may contribute unlimited amounts to SEP IRAs |
| **c.** | Employees cannot be included in SEP IRAs |
| **d.** | Taxpayers with a SEP IRA must contribute for their employees |

**See discussion of SEP IRAs in text.**

 Which of these statements concerning individual 401(k)s is false?

|  |  |  |
| --- | --- | --- |
| **a.** | In general, individual 401(k)s have higher administrative costs than SEP IRAs. | **C** |
| **b.** | Employees cannot participate in individual 401(k)s. |
| **c.** | Individual 401(k)s are available only to self-employed taxpayers with 100 or fewer employees who earn at least $5,000 a year. |
| **d.** | Individual 401(k)s have contribution limitations. |

**Individual 401(k)s are strictly for self-employed individuals who do not have employees.**

 Kathy is 60 years of age and self-employed. During the year she reported
$400,000 of revenues and $100,000 of expenses relating to her self-employment activities.
If Kathy has no other retirement accounts in her name, what is the maximum amount
she can contribute this year to a simplified employee pension (SEP) IRA?

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **a.** | $54,000  | **b.** | $51,500  | **c.** | $55,410  | **d.**  | $73,880 |  |  | **A** |

**Contributions to SEP IRAs are limited to $54,000 in 2017.**