The Different Types of IRAs

This popular retirement savings vehicle comes in several varieties.

Provided by Ed Grondahl NCU Retirement & Investment Services

What don't you know? Many Americans know about Roth and traditional IRAs, but there are other types of Individual Retirement Arrangements. Here's a quick look at all the different types of IRAs:

Traditional IRAs (occasionally called deductible IRAs) are the "original" IRAs. In most cases, contributions to a traditional IRA are tax deductible: they reduce your taxable income, and as a consequence, your federal income taxes. Earnings in a traditional IRA grow tax deferred until they are withdrawn, but they will be taxed upon withdrawal, and those withdrawals must begin after the IRA owner reaches age 70½. I.R.S. penalties and income taxes may apply on withdrawals taken prior to age 59½.[1]

Roth IRAs do not feature tax-deductible contributions, but they offer many potential perks for the future. Like a traditional IRA, they feature tax-deferred growth and compounding. Unlike a traditional IRA, the account contributions may be withdrawn at any time without being taxed, and the earnings may be withdrawn, tax-free, once the IRA owner is older than 59½ and has owned the IRA for at least five years. An original owner of a Roth IRA never has to make mandatory withdrawals after age 70½. In addition, a Roth IRA owner may keep contributing to the account after age 70½, so long as he or she has earned income. (A high income may prevent an individual from making Roth IRA contributions.)[1,2]

Some traditional IRA owners convert their traditional IRAs into Roth IRAs. Taxes need to be paid once these conversions are made.[1]

SIMPLE IRAs are traditional IRAs used in a SIMPLE plan, a type of retirement plan for businesses with 100 or fewer workers. Employers and employees can make contributions to SIMPLE IRA accounts. The annual contribution limit for a SIMPLE IRA is more than twice that of a regular traditional IRA.[3]

SEP-IRAs are Simplified Employee Pension-Individual Retirement Arrangements. These traditional IRAs are used in SEP plans, set up by an employer for employees, and funded only with employer contributions.[4]

Spousal IRAs really do not exist as a distinct IRA type. The term actually refers to a rule that lets non-working spouses make traditional or Roth IRA contributions as long as the other spouse works and the couple files joint federal tax returns.[1]

Inherited IRAs are Roth or traditional IRAs inherited from their original owner by either a spousal or non-spousal beneficiary. The rules for Inherited IRAs are very complex. Surviving spouses have the option to roll over IRA assets they inherit into their own IRAs, but other beneficiaries do not. No contributions can be made to Inherited IRAs, which are also sometimes called Beneficiary IRAs.[5]

Group IRAs are simply traditional IRAs offered by employers, unions, and other employee associations to their employees, administered through trusts.[6]

Rollover IRAs (occasionally called conduit IRAs) are IRAs created to store assets distributed from another qualified retirement plan, often an employer-sponsored retirement plan. If the original plan were a Roth, then a Roth IRA must be created for the rollover. Assets from a non-Roth plan may be rolled over into a Roth IRA, but the rollover will be viewed as a Roth conversion by the Internal Revenue Service.[6,7]

Education IRAs are now mainly referred to by their proper name: the Coverdell ESA. A Coverdell ESA is a vehicle that helps middle-class investors save for a child’s education. Taxes are deferred on the assets saved and invested through the account. Contributions to a Coverdell ESA are not deductible, but withdrawals are tax-free, provided they are used to pay for qualified higher education expenses.[8]

Consult a qualified financial professional regarding your IRA options. There are many choices available, and it is vital that you understand how your choice could affect your financial situation. No one IRA is the “right” IRA for everyone, so do your homework and seek advice before you proceed.

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Citations.

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