Steven M. Vogt, CPA, EA

How Can a Nonworking Spouse Qualify to Fund an IRA?

Article Highlights:

- Spousal IRA
- Compensation Requirements
- Maximum Contribution
- Traditional or Roth IRA?

One of the fallouts of the COVID-19 pandemic is that millions of people have dropped out of the workforce, particularly female workers with families. While they remain unemployed, these women will have lost the opportunity to build up their retirement nest egg through their employers' retirement plans. However, those who are married have an option to accumulate retirement funds that will help make up for some of their lost retirement savings.

This frequently overlooked tax benefit is the spousal IRA. Generally, IRA contributions are only allowed for taxpayers who have compensation (the term "compensation" includes wages, tips, bonuses, professional fees, commissions, taxable alimony received, and net income from self-employment). Spousal IRAs are the exception to that rule and allow a nonworking or low-earning spouse to contribute to his or her own IRA, otherwise known as a spousal IRA, as long as his or her spouse has adequate compensation.

The maximum amount that a nonworking or low-earning spouse can contribute to either a traditional or Roth IRA (or a combination) is the same as the limit for a working spouse, which is $6,000 for 2021. If the nonworking spouse is 50 years or older, that spouse can also make "catch-up" contributions (limited to $1,000), raising the overall contribution limit to $7,000. These limits apply provided that the couple together has compensation equal to or greater than their combined IRA contributions.

> ***Example:*** *Tony is employed, and his W-2 for 2021 is $100,000. His wife Rosa, age 45, didn't work during the year after deciding to care for their children at home due to their difficulty finding childcare providers. Since her own compensation of zero is less than the contribution limit for the year, Rosa can base her contribution on their combined compensation of $100,000. Thus, Rosa can contribute up to $6,000 to an IRA for 2021. Even if Rosa had done some part-time work and earned $2,500, she could still make a $6,000 IRA contribution.*

The contributions for both spouses can be made either to a traditional or Roth IRA or split between them as long as the combined contributions don't exceed the annual contribution limit. **Caution:** The deductibility of the traditional IRA and the ability to make a Roth IRA contribution are generally based on the taxpayer's income:

- **Traditional IRAs** – There is no income limit restricting contributions to a traditional IRA. However, if the working spouse is an active participant in any other qualified retirement plan, a <u>tax-deductible</u> contribution can be made to the IRA of the nonparticipant spouse only if the couple's adjusted gross income (AGI) doesn't exceed $198,000 in 2021. If the couple's income is $198,000 to $208,000, only a partial deduction is allowed. Once their AGI reaches $208,000, no amount is deductible.

- **Roth IRAs** – Roth IRA contributions are never tax-deductible. Contributions to Roth IRAs are allowed in full if the couple's AGI doesn't exceed $198,000 in 2021. The contribution is ratably phased out for AGIs between $198,000 and $208,000. Thus, no contribution is allowed to a Roth IRA for 2021 once the AGI exceeds $208,000.

> ***Example:*** *Rosa from the previous example can designate her IRA contribution as either a*

deductible traditional IRA or a nondeductible Roth IRA because the couple's AGI is under $198,000. Had the couple's AGI been $203,000, Rosa's allowable contribution to a deductible traditional or Roth IRA would have been limited to $3,000 because of the phaseout. The other $3,000 could have been contributed to a traditional IRA and designated as nondeductible.

Contributions to IRAs for 2021 can be made no later than April 15, 2022.

Please give this office a call if you would like to discuss IRAs or need assistance with your retirement planning.