Your Firm LLC

The Benefits of a Spousal IRA

When it comes to Individual Retirement Accounts (IRAs), a common misconception is that they are only available to people who are employed. While IRAs do have certain income requirements, a Spousal IRA enables a spouse who is unemployed to contribute to an IRA

What is a Spousal IRA?

An individual's annual contributions to an IRA cannot exceed their earned income for such year. This would normally prohibit a spouse with low or no earnings from contributing to an IRA. However, 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.

To qualify, the unemployed spouse must be legally married, they must file a joint tax return and their combined income must meet certain requirements.

A Spousal IRA is not a specific type of IRA, but more of a rule on how an unemployed spouse can contribute to an IRA. The actual retirement account may be a traditional IRA, a Roth IRA, or a combination of the two.

Even though a spousal IRA is funded from the employed spouses' income, it must be owned and controlled by the unemployed spouse. It cannot be jointly held. However, both spouses can have their own IRAs.

Contribution Limits

The primary reason for setting up a Spousal IRA is so the couple can save more for retirement.

For 2021, the annual contribution limit for IRAs is $6,000. Individuals who are age 50 or older are allowed to make an additional "catch-up" payment which is limited to $1,000. Thus, a couple could theoretically contribute up to $14,000 a year to their IRAs.

There are two limits on contributions to an IRA though. First, the total contributions a couple may make to their IRA accounts may not exceed their combined taxable income for the year. Second, contributions to a Roth IRA become limited if a couple's combined income exceeds a certain amount.

Tax Deductions

Contributions to a traditional IRA are generally tax-deductible, but the amount a spouse can deduct may be limited. If the working spouse is covered by their employer's retirement plan and the couple's combined modified adjusted gross income does not exceed $104,000 in 2021, then they can deduct the full amount of their contributions. This deductibility starts to phase out between $104,000 and $124,000 and is unavailable if their modified adjusted gross income is greater than $124,000.

Contributions to a Roth IRA are made post-tax, so there are no immediate tax benefits from the contributions.

Contribution Deadlines

The deadline to contribute to all IRAs including spousal IRAs usually coincides with the tax filing deadline, which is typically April 15th. You can make a contribution for the year 2021 anytime until April 15, 2022. Also, up until the tax filing deadline each year, contributions can be made for the current year or previous year.

Additional Considerations

Although it is fairly common for IRA account holders to designate a surviving spouse as the primary beneficiary of the IRA, it is advised that one takes a lot of care when designating beneficiaries for a spousal IRA account and review it periodically. It is also advisable to discuss desired beneficiaries with a personal attorney due to distribution rules for IRA inheritors set by the SECURE Act.

Ultimately, although spousal IRAs have tax-saving benefits, they may not be right for everyone. These are usually intended for long-term investments and as a result, withdrawing early from an IRA can lead to penalties, which often include a higher tax bracket. However, there are exceptions that can permit early withdrawals without a tax penalty.

Next Steps

This document is meant to provide an overview of a Spousal IRA and is not a substitute for speaking with one of our advisors. If you would like to learn more about how a spousal IRA works and learn if it is right for you, reach out to our office at any time.

About Your Firm LLC

We have hand-picked a team with tax, auditing, accounting, business and management advisory expertise in a multitude of fields, including healthcare, professional-services firms, commercial contractors, home builders, real estate companies, manufacturing and distribution companies, dealerships, non-profit organizations and pension funds.

We have the expertise and the resources to provide not only the critical services you need during these evolving economic times, but also, importantly, to build for the future. Our strategic alliances with professional organizations across the country allow us to bring our clients the talent and expertise of national firms with the high-touch service of a local firm. While we remain focused on the core services of tax, accounting and audit, we expand and offer you the business consulting needed to remain competitive. We believe the success of our clients is the greatest measure of our own.

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