

## **New Tax Law Includes Changes to Roth IRAs and Capital Gains**

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On May 17, 2006, President Bush signed a new tax bill into law which makes a number of changes to tax law, including who can participate in a Roth IRA, extending the capital gains tax reduction, making unearned income by minors up to age 18 taxable at the parent's tax rate and increasing the Alternative Minimum Tax exemption.

The new law increases the number of people who can participate in a Roth IRA. With a Roth IRA, unlike a traditional IRA, you do not receive a tax deduction when you invest your money, but your original deposits and the earnings on them are not taxed when you withdraw the funds. However, not everyone can participate in a Roth IRA. Individuals with income of more than \$110,000 and couples with more than \$160,000 cannot put money into a Roth IRA. Furthermore, households with incomes of more than \$100,000 cannot convert a Traditional IRA into a Roth IRA.

The new law, which takes effect in 2010, does not change the income threshold for people who are starting a new Roth IRA, but it will allow people with income of more than \$100,000 to convert a Traditional IRA into a Roth IRA. While you will have to pay taxes on the conversion, if you convert in 2010, you could split the taxes into two payments to be paid in 2011 and 2012. If you convert after 2010, you will have one year to pay the taxes.

The new tax law also extends the capital gains tax reduction passed in 2003. The reduction was supposed to be effect only until 2008, but the new law extends the rate until 2010. The tax rate on taxpayers in the highest tax brackets will remain at no more than 15%. Taxpayers in the 10% and 15% tax bracket will pay a 5% rate until 2007, and, starting in 2008, they won't have to pay any capital gain taxes when they sell assets, such as stocks and mutual funds.

Another change in the tax law may affect seniors who have opened custodial accounts (or UTMA account) for their grandchildren. The new law makes unearned income by minors up to age 18 taxable at the parent's tax rate. Previously, the first \$850 of investment gain from a custodial account was tax free, the second \$850 was taxed at the child's rate, and any income over that was taxed at the parent's or grandparent's rate. When a child turned 14, anything over \$850 was taxed at the child's rate. Under the new law, any income over \$1,700 is taxed at the parent's or grandparent's rate until the child turns 18.