



**MLK Capital Management, Inc.**

**Individual  
Retirement Account  
Guide**

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**Traditional IRA**

**Roth IRA**

**Education IRA**

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# **Look at your Individual Retirement Account (IRA) Options**

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The Taxpayer Relief Act of 1997 created a variety of new IRA options. Not only did it change rules for the traditional IRA, but it also introduced the Roth and Education IRAs. These options were improved by the Economic Growth and Tax Relief Reconciliation Act of 2001.

Traditional IRAs are more attractive than ever because expanded income limits mean more people will be able to make tax-deductible contributions. In addition, penalty-free withdrawals are allowed for qualified higher-education expenses and for a first-time home purchase.

Contributions to the Roth IRA or Education IRA (now known as the Coverdell Education Savings Account) aren't tax-deductible, but the accounts offer the opportunity for tax-free earnings.

Your tax adviser can offer more guidance on which type of IRA may be best for your needs. Of course, we are always here to answer your questions and assist you with opening an IRA. Please call us today at (713) 993-0949 for more information.

Traditional, Roth, or Educational IRA? Which is best for you?

## Roth IRA



### Who can contribute?

- Anyone who has income from compensation (or who is filing jointly with a spouse who earns compensation) with the following MAGI:\*
  - Up to \$95,000 (single filers)
  - Up to \$150,000 (joint filers)
- Reduced contributions allowed for higher incomes (up to \$110,000 for single filers and \$160,000 for joint filers)

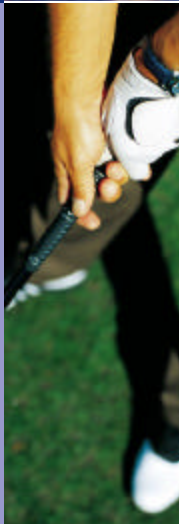
### How much can I contribute?

- \$3,000 for 2004
- Higher limit if age 50 or older
- Cannot exceed compensation
- Reduced by contributions to Traditional IRAs

### What are the tax advantages?

- Regular contributions can be withdrawn tax- and penalty-free at any time
- After the account has been open five tax years, earnings can be withdrawn tax- and penalty-free for any of these reasons: age 59-1/2, disability, death, or a first-time home purchase\*\*

## Traditional IRA



- Anyone under age 70-1/2 who has income from compensation (or who is filing jointly with a spouse who earns compensation)

- \$3,000 for 2004
- Higher limit if age 50 or older
- Cannot exceed compensation
- Reduced by contributions to Roth IRAs

- Earnings grow tax-deferred until withdrawn
- Contributions may be tax-deductible

## Education IRA\*\*\*



- Anyone who has MAGI\* - Single filer: up to \$95,000 - Joint income for filers: up to \$190,000
- People with higher MAGI may be able to make smaller contributions
- Contributions not allowed after the beneficiary reaches age 18 (contributions after age 18 allowed for special-needs beneficiaries)

- \$2,000 per child
- Limit applies to all Education IRAs for the same child

- Withdrawals for certain qualified education expenses are tax-free
- Special-needs beneficiaries can withdraw funds tax-free to pay for qualified education expenses at any age
- Qualified education expenses may include tuition, fees, books, computer equipment required for elementary, secondary and post-secondary education
- A beneficiary may receive tax-free distributions from an Education IRA in the same year he or she claims the Lifetime Learning or HOPE Scholarship tax credits

\*MAGI - modified adjusted gross income from the federal tax form

\*\* Lifetime limit for exemption on first-time home purchase is \$10,000

\*\*\* Now known as the Coverdell Education Savings Account

# Traditional IRAs



## What is a traditional IRA?

A traditional IRA is a type of retirement plan that has been in existence since 1975. Traditional IRAs offer tax-deferred earnings, and the possibility for tax-deductible contributions. These tax advantages make the traditional IRA a powerful tool in creating a balanced, long-term savings plan.

## How does the traditional IRA work?

You can contribute to a traditional IRA if you earn compensation and you will not reach age 70-1/2 by the end of the year. If you file a joint tax return, you can treat your spouse's compensation as your own (except your combined contributions cannot exceed your combined compensation). All earnings in the traditional IRA are not taxed until they are withdrawn. The ability to defer taxes on the earnings, and to withdraw in a year when you may be in a lower tax bracket, can mean more after-tax dollars for your retirement.

## How much can I contribute to a traditional IRA?

If you meet the eligibility tests described above and you are under age 50, you can contribute up to \$3,000 for 2002 through 2004. If you have attained age 50 by the end of the year, then your limits are \$2,000 for 2001, and \$3,500 for 2002 through 2004. These limits are even higher for later years.

## Can I still contribute to a traditional IRA if I participate in an employer-sponsored retirement plan?

Yes, your participation in an employer-sponsored retirement plan will not affect your ability to contribute to a traditional IRA (assuming age and compensation requirements are met). However, higher-income earners will lose their ability to deduct their traditional IRA contributions if participating in an employer-sponsored plan.

## If I already have a Roth IRA, can I have a traditional IRA, too?

Yes, you can. However, the limits on annual contributions described on the previous page apply to any combination of traditional and Roth IRA contributions that you make for the year.

## How much can I deduct?

If you are single, or married and neither spouse is an active participant in a retirement plan, your traditional IRA contribution is deductible regardless of income. If you or your spouse is an active participant, you may deduct contributions only if your income is below certain limits. Smaller deductions are available if your income is within the phase-out range, which is determined by your filing status. Higher-income earners with retirement plans may still contribute, but deductions are not available if income is over the phase-out range. If you have questions about your specific tax situation, please consult your tax advisor for an interpretation of how these rules apply to you.

## Can I get any tax credits for making IRA contributions?

You may be able to receive a tax credit for making contributions for the 2002 through 2006 tax years. The amount of the deduction changes depending on whether or not you participate in your employer-sponsored retirement plan, your annual income, and filing status. Please see your tax advisor for additional information.

# Traditional IRAs

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## **Will I owe income taxes when I withdraw from my traditional IRA?**

Yes, you will owe income taxes when you withdraw from your traditional IRA. However, if you make non-deductible contributions to a traditional IRA, a portion of each withdrawal will be treated as the nontaxable return of those contributions.

## **If I make an early withdrawal from my traditional IRA before age 59-1/2, do I pay a penalty?**

In general, you must pay a 10 percent tax on early distributions or withdrawals before age 59-1/2. But the early distribution tax does not apply in the following situations:

- a. Amount is rolled over or directly transferred to another traditional IRA.
- b. Amount is properly converted to a Roth IRA.
- c. Withdrawal of an excess contribution before the tax return is due.
- d. Payment is made to your beneficiaries after your death
- e. Withdrawal of up to \$10,000 is for first-time home purchase.
- f. Amount is used to pay for qualified post secondary education expenses.
- g. Amount is used to pay for medical expenses in excess of 7.5 percent of adjusted gross income.
- h. Amount is for pre-59-1/2 periodic payments.
- i. Distribution is to an owner who is disabled (as defined by the IRS code).
- j. Distribution is for medical insurance premiums during unemployment that lasts 12 weeks or longer.

## **When must I begin taking distributions from my traditional IRA?**

You must begin taking required minimum distributions from your traditional IRA at age 70-1/2. The minimum distributions each year will be computed using an IRS formula. You are allowed to delay the first year's payment until April 1 of the following year, but you will receive two year's worth of payments in your 71-1/2 year if you choose to delay.

## **Can I move funds from a qualified retirement plan to a traditional IRA?**

If you are entitled to receive an eligible rollover distribution from an employer's plan, you can continue deferring taxes by moving the money into a traditional IRA. The best way to do this is to inform the plan administrator that you want the funds moved directly to your traditional IRA in a direct rollover. The plan administrator will inform you before making an eligible rollover distribution.

## **Can I move money from a traditional IRA to a Roth IRA?**

You can move money from your traditional IRA to a Roth IRA if your adjusted gross income for the year is \$100,000 or less, and you are either single or married filing a joint tax return. In the year you convert, you will have to pay federal income taxes on the amount that you move, except the portion that is treated as the return of your nondeductible contribution. You may also be subject to state income taxes.

## **What happens to my traditional IRA after my death?**

You may designate one or more beneficiaries to receive your IRA after your death. If your spouse is your beneficiary, he or she may direct transfer your traditional IRA to his or her own IRA tax-free. In addition, all beneficiaries have the option of taking a lump-sum payment, and in many cases, will be able to take periodic payments over a number of years. Any tax-deferred money in your traditional IRA at the time of death will be taxed when it is distributed to your beneficiaries.

*This is not intended as tax advice.  
Please consult a tax professional.*

# Roth IRAs



## What is the Roth IRA?

The Roth IRA is an individual retirement account created by the Taxpayer Relief Act of 1997. Named for former Senate Finance Committee Chairman William Roth, Jr., this IRA offers more incentives to boost your retirement savings, as well as more ways to use your nest egg.

## How does the Roth IRA work?

Unlike traditional IRA's, your contributions to the Roth IRA are never tax-deductible. However, the money in your Roth IRA, including earnings, can be withdrawn tax-free. Of course, you must conform to the plan provisions to get this tax-free advantage.

## Am I eligible to contribute to a Roth IRA?

You are eligible if you earn compensation and your income is less than limits set by Congress. A single filer who has modified adjusted gross income (MAGI) up to \$95,000 can make the full Roth IRA contributions for that year. Each spouse filing a joint federal income tax return showing a MAGI up to \$150,000 can make the full Roth IRA contributions for that year. Some people with higher MAGI may be able to make smaller contributions.

## How much is the full Roth IRA contribution?

The amount of a full Roth IRA contribution varies. If you meet the eligibility tests described above and you are under age 50, you can contribute up to \$3,000 for 2002 through 2004. If you have attained age 50 by the end of a year, then your limit is \$3,500 for 2002 through 2004. These limits are even higher for later years.

## What happens if my (our) income is too high to make a full contribution to a Roth IRA?

A portion of the full contribution can be made if your MAGI is between \$95,000 and \$110,000 for single filers, and between \$150,000 and \$160,000 for joint filers. When income exceeds \$110,000 for single filers and \$160,000 for joint filers, a regular Roth IRA contribution can't be made for that year.

## Can I get any tax credits for making IRA contributions?

You may be able to receive a tax credit for making contributions for the 2002 through 2006 tax years. The amount of the deduction changes depending on whether or not you participate in your employer-sponsored retirement plan, your annual income, and filing status. Please see your tax advisor for additional information.

## Can I still contribute to a Roth IRA if I participate in an employer-sponsored retirement plan?

Yes, and you can contribute past age 70-1/2 as long as you continue to earn compensation.

## Will my Roth IRA affect the amount that I can contribute to my employer-sponsored retirement plan?

No. The amount you contribute to your 401(k) or other employer-sponsored plans will not be affected by your Roth IRA. However, you must conform to the plan contribution limits for your employer-sponsored plan.

## Can I have both a traditional and a Roth IRA?

Yes, you can maintain both types of IRAs at the same time. You can even make contributions to both types of IRAs in the same year. But your contributions to both Roth and traditional IRAs cannot exceed the maximum contribution limit for all IRAs.

# Roth IRAs

## **When can I start taking tax-free distributions from my Roth IRA?**

You can withdraw most contributions without paying income tax at any time. Distributions are treated as first being attributable to your contribution until all of your contributions have been distributed.

There are two requirements to qualify for tax-free withdrawals of the income your Roth IRA has earned. First, your Roth IRA must meet a “five-year test.” In other words, it must be five years after the first year for which Roth contributions were made. Second, one of the following conditions must apply:

- a. You are over age 59-1/2.
- b. Funds are going to your beneficiary upon your death.
- c. You have become disabled.
- d. You are using the funds for a first-time home purchase (lifetime limit is \$10,000 per person).

If you have made a conversion contribution, please read further for taxation issues regarding conversions in this situation.

## **What if I make an early withdrawal from my Roth IRA and I am not age 59-1/2 or covered by any exceptions?**

Good news. If you make early withdrawals from a Roth IRA to which you have only made regular contributions of up to \$3,000 per year, the amounts are considered to come from your already-taxed contributions first, with no additional taxes or penalties due. When you begin to withdraw earnings from the account, the money will be subject to ordinary income taxes plus an additional 10 percent early distribution tax.

## **Do I have to take minimum distributions when I reach age 70-1/2?**

No. The Roth IRA is more flexible than a traditional IRA because you are not required to start taking minimum distributions when you reach age 70-1/2. If you don't need the cash, you can let your money continue to grow tax-free for as long as you like. However, minimum distributions must be made to your beneficiaries following your death.

## **Can I convert my existing traditional IRA to a Roth IRA?**

Yes. You can convert your traditional IRA to a Roth IRA if your MAGI in the year of the conversion is under \$100,000. This limit is the same for both single filers and married couples who file jointly. Married taxpayers who file separately are not eligible for a Roth conversion. Use care and be sure to get all the facts. This is a complicated decision.

## **Does the IRA conversion contribution ceiling of \$100,000 MAGI include the IRA conversion amount?**

No, the MAGI is calculated prior to adding the amount of the IRA conversion contribution.

## **If I convert a traditional IRA to a Roth IRA, do I owe any taxes?**

Yes. Upon conversion, you will owe ordinary income taxes on your investment earnings and on deductible contributions you have made to your traditional IRA. This amount is taxable income in the year the money leaves the traditional IRA. Basically, you owe tax on any money that has not been taxed before. But you will have the opportunity to withdraw earnings made after the conversion, free of any taxes.

## **What about penalties on conversions from traditional IRAs to Roth IRAs?**

The 10 percent early withdrawal penalty is waived on IRA conversions.

## **Are there different tax rules regarding withdrawals of IRA conversion contributions?**

A distribution that is attributed to an IRA conversion contribution is not subject to income tax. If the distribution is made within five years after the conversion, then the 10 percent early withdrawal tax applies unless there is an exception.

# Roth IRAs

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## **Can I roll over funds from one Roth IRA to another Roth IRA?**

Yes. A rollover or transfer from one Roth IRA to another Roth IRA is tax-free and can be made regardless of your MAGI.

## **What should I do if I am eligible for both a Roth IRA and my company retirement plan, but I don't have enough money to contribute the maximum to both?**

Experts recommend that you first contribute at least enough to your company plan to take full advantage of any employer match. After getting the full employer match, the best approach varies depending on your circumstances. Consult with a tax professional if you are unsure.

## **Does it make sense to make an after-tax voluntary contribution to my company retirement plan instead of a Roth contribution?**

Not necessarily, you may have more nontaxable income upon retirement by making Roth IRA contributions.

## **Does it make sense to make a nondeductible contribution to a traditional IRA instead of a Roth contribution?**

Not necessarily, you could have a better tax result by making a Roth IRA contribution.

## **What if I can deduct a contribution to a traditional IRA?**

In general, a person who can afford to make the maximum Roth IRA contribution will benefit more from making Roth IRA contributions. This may not be true if you are close to retirement and it appears that your tax bracket will go down substantially after retirement. You should also consider a deductible traditional IRA contribution if losing the deduction would reduce the amount you can contribute. Seek tax advice if you are in doubt.

## **Can my Roth IRA be inherited?**

Yes. Upon your death, the entire proceeds can be passed on tax-free to your beneficiaries, once the five-year test has been met. This means there may be a delay before your beneficiaries will be able to receive the income earned within the Roth IRA on a tax-free basis.

## **How will I know if I am a good candidate to convert my traditional IRA to a Roth IRA?**

The desirability will differ with each individual's financial circumstances. Certainly, you should weigh the potential tax savings during retirement against the cost of your tax bill for the conversion. Because this decision is a complicated one, you should consult a tax professional.

Consider several key questions:

- Is your IRA comprised mostly of already taxed, nondeductible contributions?
- Can you afford to pay the income taxes due on the conversion from funds outside of your IRA funds?
- What tax bracket are you in now, and what tax bracket do you think you will be in when you retire?
- How long is it before you retire?
- Will the taxable income from your conversion bump you into a higher tax bracket?
- How will the income from your conversion affect the taxation of any Social Security retirement benefits you receive?

## **I know about the federal tax due on Roth accounts, but what about state taxes?**

In many states, treatment of the Roth IRA for state tax purposes is the same as the treatment of the account for federal tax purposes by the IRS. Consult your tax adviser for more information on state taxes for the Roth IRA.

*This is not intended as tax advice.  
Please consult a tax professional.*

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# Education IRAs

Coverdell Education Savings Account



## What is the Education IRA?

The Education IRA, recently renamed the Coverdell Education Savings Account, is a type of tax-advantaged savings account created by the Taxpayer Relief Act of 1997. This IRA's sole purpose is to help you pay for your child's education expenses such as: tuition, fees, books, supplies, equipment, and, in some cases, room and board and computers. These options were improved by the Economic Growth and Tax Relief Reconciliation Act of 2001.

## How does the Education IRA work?

Unlike traditional IRAs, your contributions to an Education IRA are never tax-deductible. However, an Education IRA offers you the potential for tax-free withdrawals – including earnings. Here's a look at how your money can grow in an Education IRA:



No taxes are due on withdrawals used for qualified higher-education expenses

## What is the most I can contribute to an Education IRA?

The total contributions each year to each child's Education IRA cannot exceed \$2,000 for 2002 and later years. If you're eligible, you can contribute the full amount for each child. For example, if you have three children and each has his or her own Education IRA, you can contribute \$6,000 for 2002 (\$2,000 to each IRA).

## Who is eligible to open and contribute the full amount to an Education IRA?

You can contribute the full amount if you are a:

- Single filer with modified adjusted gross income (MAGI) up to \$95,000.
- Joint filer with MAGI up to \$190,000 for 2002 and later years.

## What happens if my (our) income is too high to make the full contribution to an Education IRA?

You can make contributions of less than the full amount if you are a:

- Single filer with MAGI between \$95,000 and \$110,000.
- Joint filer with MAGI between \$190,000 and \$220,000 for 2002 and later years.

If your income exceeds these amounts, you cannot make a regular Education IRA contribution for that year.

## How long can I contribute to the account?

You can make contributions to a child's Education IRA until he or she reaches the age of 18. For 2002 and later years, this age limit does not apply to special-needs beneficiaries. This is a person who requires additional time to complete his or her education because of a physical, mental or emotional condition (including a learning disability).

## As a parent, am I the only one who can open and contribute to an Education IRA for my child?

No. Anybody who meets the income requirements can open and contribute to your child's Education IRA. This includes grandparents, aunts and uncles, family friends, and anyone else who wants to pitch in to your child's education fund. Starting in 2002, corporations, tax-exempt organizations, and other entities can also make Education IRA contributions, and there are no income limits on these contributors. However, the total contributions to all Education IRAs for each child can't exceed \$500 for 2001, or \$2,000 for 2002 and later years.

## Who controls the account?

Every Education IRA must have one, and only one "responsible individual" to oversee the account. This person decides when funds will be withdrawn and if and when funds will be rolled over to the Education IRA of a family member. You can be the "responsible individual" as long as you are a parent or legal guardian of the child.

# Education IRAs

## **When can I withdraw funds from an Education IRA?**

As the responsible individual, you can withdraw funds at any time. However, to avoid tax consequences from the withdrawal, you must use the funds to pay for qualified education expenses for your child (the IRA's designated beneficiary) before he or she reaches age 30 (except that the age 30 limit does not apply to a special-needs beneficiary).

## **What educational expenses are considered to be "qualified?"**

Qualified expenses include tuition, fees, books, and equipment required for enrollment or attendance at nearly any post-secondary education institution (public, nonprofit or proprietary). Certain room and board expenses also may qualify. Starting in 2002, qualified expenses also include these same expenses for elementary and secondary education, and the purchase of computer technology or equipment that is used by the beneficiary and the beneficiary's family while the beneficiary is in school.

## **What happens if my child doesn't use the funds?**

If your child (the designated beneficiary of the IRA) decides not to go to college or leaves school before all the funds are withdrawn, you can roll unused funds into the Education IRA of another child in your family. The beneficiary of the Education IRA that receives the unused funds must be under the age of 30 (except that the age 30 limit does not apply to a special-needs beneficiary).

## **Who is considered a family member for the purposes of rollover?**

Family members of the designated beneficiary who are eligible to receive unused funds include (but are not limited to) spouses, siblings, stepsiblings, nieces, nephews, parents, aunts, uncles, grandparents, children, and grandchildren. Of course, some of these categories will be eliminated immediately since the new designated beneficiary must be under the age of 30 at the time of the rollover (except that the age 30 limit does not apply to a special-needs beneficiary).

## **What if my child earns an academic scholarship and the tuition is waived?**

The amount of scholarship money your child receives is deducted from the allowable expenses for the Education IRA. For example, if qualified expenses total \$6,000 and your child receives a scholarship for \$3,000 you can make a qualified withdrawal of \$3,000 from the Education IRA. Remember that unused funds can always be rolled over to a family member.

## **Can I roll funds from a traditional or Roth IRA into an Education IRA?**

No, rollovers from a traditional or Roth IRA into an Education IRA are not allowed.

## **How does the Education IRA affect other education savings incentives?**

In 2002 and later years, contributions can be made on behalf of the same child to both an Education IRA and a qualified prepaid state tuition program. In 2002 and later years, a person can also receive tax-free distributions from an Education IRA in the same year he or she claims the Lifetime Learning or HOPE Scholarship tax credits, but the same expenses cannot be used for more than one of these tax benefits.

## **If I contribute to an Education IRA, can I still contribute to a traditional or Roth IRA?**

Contributions to traditional or Roth IRAs have no effect on the contribution you can make to each Education IRA.

## **Don't traditional and Roth IRAs allow me to withdraw funds for education expenses?**

Traditional and Roth IRAs do offer penalty-free withdrawals for qualified higher-education expenses, but you may still need to pay taxes on those withdrawals. In contrast, withdrawals from an Education IRA are both tax-free and penalty-free if used for qualified education expenses.

**MLK Capital Management, Inc.**

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www.401k-Investment-Advice.com

Address Service Requested

**Complete and return this form ASAP to get more information about opening an IRA.....**

**Hurry! The tax deadline is April 15th!**

**Return this form to:**

**MLK Capital Management, Inc.  
5075 Westheimer, Suite 1177, Houston, TX 77056  
(713) 993-0949—local  
(800) 945-2125—toll free  
(713) 993-0950—fax**

Name: \_\_\_\_\_

Social Security Number: \_\_\_\_\_

Address: \_\_\_\_\_

City, State, Zip: \_\_\_\_\_

Home Phone: \_\_\_\_\_

Work Phone: \_\_\_\_\_

E-mail Address: \_\_\_\_\_

Date of Birth: \_\_\_\_\_

Best time to call: \_\_\_\_\_

Please contact me with more information about:

- Traditional IRAs
- Roth IRAs
- Education IRAs