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ADVISOR THOUGHTS

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RETIREMENT ACCOUNTS: RECENT CHANGES & THE BEST WAYS TO ADJUST YOUR STRATEGIES

[Whenever you are planning dealing with IRS rules and regulations that impact your tax situation, you should consult with your attorney or tax advisor. This article does not constitute tax or legal advice, but provides a general overview of the recent changes to the IRA rules.]

Normally people who have Individual Retirement Accounts (IRAs) must take a required minimum distribution (RMD) beginning when they are age 70 ½. The SECURE and CARES Acts adopted by Congress this year changed that requirement in a couple of significant ways. First, account owners of IRAs now have until the age of 72 to start required distributions. Second, the Act eliminated the requirement of taking a minimum distribution for the year 2020 regardless of your age. Moreover, the waiver of your 2020 minimum distributions covers both IRA account owners and the beneficiaries of inherited IRAs.

Notwithstanding the fact that you do not need to take a RMD this year, should you still take one?

When you take funds from an IRA, the distribution is subject to taxation at your ordinary income tax rate. If you were to leave these funds in the IRA instead, they would continue to grow tax deferred. As a result, it is generally better to leave the funds in your IRA and use other types of accounts if you need money. However, there are exceptions to this rule:

- First, you may need the funds for living expenses. If you have other sources of income, you might be able to rely on these more heavily and at least reduce the amount being withdrawn from your IRA this year. If you have some cash in a savings account, now might be the time to tap into it. Alternatively, if your other sources of income include appreciated stock, you will need to weigh the cost of paying capital gains at a tax rate of 15-20% versus withdrawing from your IRA at your marginal income tax rate.

- Second, you or your CPA may decide it is better to take a partial distribution this year if you are trying to smooth out your income each year and the RMD withdrawal would not push you into a higher tax bracket.

- Third, if you have been using your RMD for charitable giving (i.e. a qualified charitable distribution), you or your financial advisor will need to evaluate your options. While it is generally better to use RMD for charitable giving because you save more in taxes, this year you have the option of keeping those funds invested in your IRA to continue to grow tax deferred. Instead, you could use cash or appreciated stock. However, whether this is a better strategy for gifting will depend on a number of factors. You or your financial advisor should consider the relative value of the stock market at the time of the gift, the amounts of charitable deductions available for appreciated stock versus other types of assets, and the impact of the charitable giving on any existing plans to fund cash flow needs.

What happens if I have already taken my RMD this year?

The CARES ACT also expanded the ability to rollover or pay back distributions already taken from an IRA. Normally, an IRA owner or beneficiary has 60 days to rollover or to return a prior distribution made to them back into the distributing IRA, and they can only do this only once every 12 months. While these rules are still in effect, the CARES ACT has given IRA owners and beneficiaries extra benefits: a recipient of an IRA RMD distribution made in 2020 is now allowed to repay the amount to their IRA at any time so long as it gets into the account by August 31, 2020. Moreover, if you received multiple RMD distributions, you may make multiple rollovers because the IRS is no longer counting rollovers of 2020 RMD made by August 31st, 2020 in the only one rollover per 12 months rule.

These changes give IRA owners greater flexibility in managing their repayments. For example if you take a RMD distribution from your IRA in July or August, you have until the later of August 31st or 60 days to get the rollover repayment into your account, but if you get it in by August 31st, it should not count toward the only one rollover every 12 months rule.

Valerie J. Nevel
Senior Financial Advisor & Fiduciary Consultant
Valerie.nevel@ledyardbank.com