

RMD's and Taxes, Social Security, Roth IRA, ...

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This Presentation Is Not Tax Advice

- The purpose of this presentation is to share my understanding of Required Minimum Distributions.
- I am not a tax professional.
- This presentation should not be taken or relied upon as tax advice.
- Only general features of Required Minimum Distributions are contained in this presentation. The tax law includes many details and a number of special cases which can affect the tax treatment of distributions.
- Everyone's tax situation is different. For proper tax advice, consult a qualified tax professional.

Agenda

“Nothing can be said to be certain, except death, taxes, and RMD’s”
– updating B. Franklin

- What are RMD’s
- Impact of RMD’s
 - Income Taxes
 - Social Security
 - Medicare
- Mitigating RMD’s
 - Charitable Contributions
 - Roth Conversions

RMDs - Required Minimum Distributions

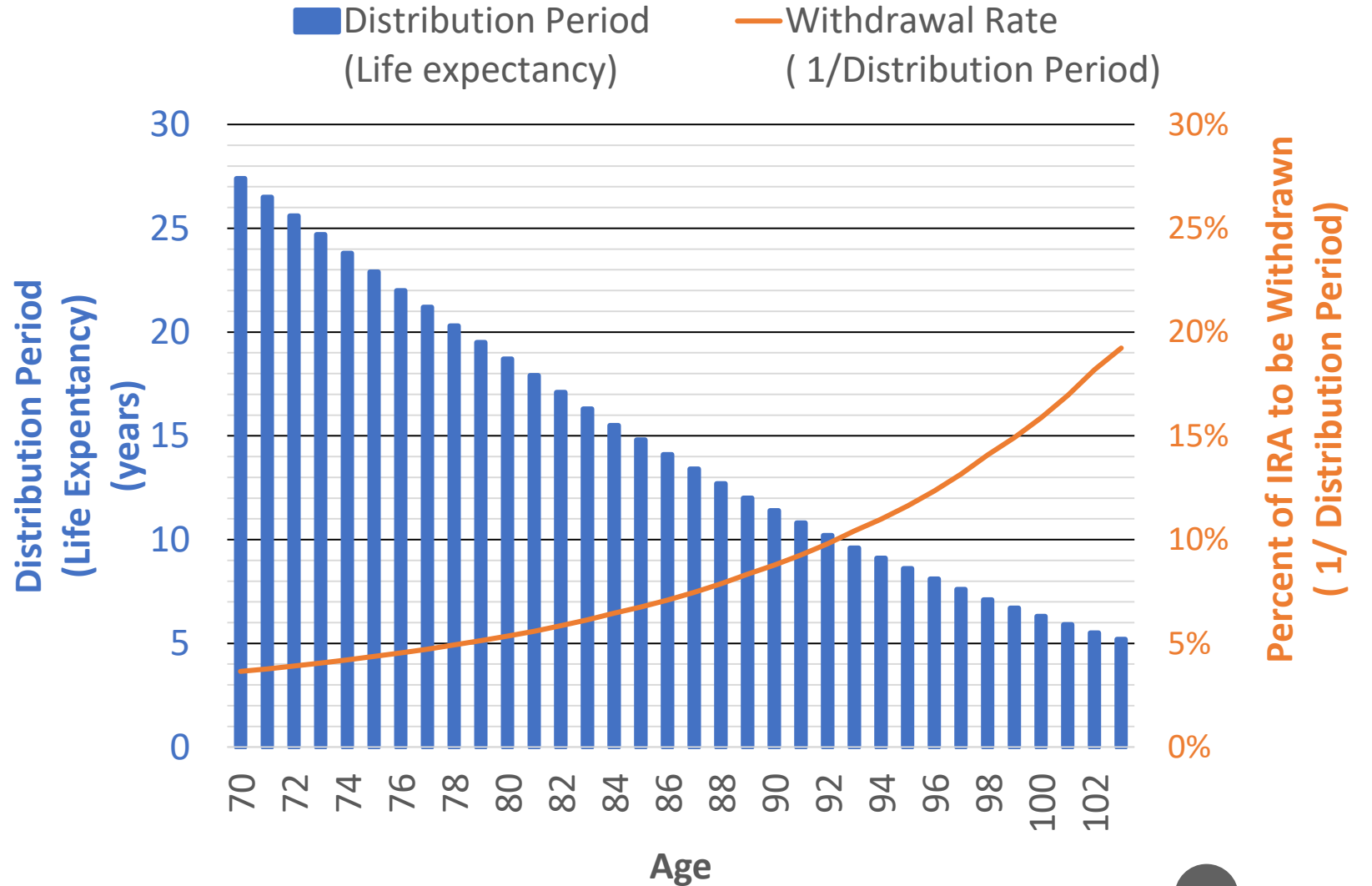
1. Distributions from your traditional IRA begin the year you turn 70 ½ and continue every year after that
 - First Year: Distributions from your IRA must begin by April 1st of the year after the year in which you reach 70 ½ .
 - Following Years: Distributions must be taken by December 31st of that year.
2. Distributions from IRA's are taxable as ordinary income in the year you receive them.
 - Distributions from an IRA include your contributions, capital gains, dividends, and interest. Everything is treated the same for tax purposes.
 - Distributions can be taken as cash or re-invested in a taxable investment account – don't have to be spent
 - RMD distributions cannot be moved into another tax-deferred account (e.g. Roth IRA)
3. The amount of the RMD depends upon the IRA account balance and the applicable IRS life expectancy
 - IRA account balance: Value of the IRA on December 31st of the year before the year the distribution is due.
 - E.g. the basis for your 2019 RMD is the value of your IRA on December 31, 2018.
 - IRS life expectancy: the Life Expectancy or Distribution Period given in IRS Pub 590-b Tables I, II, or III.
 - RMD amount = (IRA account balance) / (IRS life expectancy)

IRS Withdrawal Rates for IRA's

(Pub 590b, Table III: Single IRA owners and Married Owners whose Spouses aren't More than 10 Years Younger)

Example RMD's for \$ 1,000,000 IRA

Age	Distribution Period (yrs)	RMD Amount
70	27.4	\$ 36,496
75	22.9	\$ 43,668
80	18.7	\$ 53,476
85	14.8	\$ 67,568
90	11.4	\$ 87,719



Example of Fred and Wilma

- Fred turns 70 on February 20, 2019 and so reaches 70 ½ on August 20, 2019.
- The value of Fred's traditional IRA on December 31, 2018 was \$ 1,000,000.
- Fred's wife Wilma is three years younger than Fred.
- Fred's RMD is computed from IRS Pub 590b, Appendix B, Table III as
 - $\text{Distribution Period} = 27.4 \rightarrow \text{RMD} = \$ 1,000,000 / 27.4 = \$ 36,496.$ (about 3.65% of the value of his IRA)
- Fred must take his first RMD by April 1, 2020.
- Fred must take his second RMD by December 31, 2020 and so forth for following years.
- Fred should consider taking his first RMD in 2019, otherwise he will pay taxes on a two RMD's in 2020
 - One RMD in 2019 and one in 2020 \rightarrow RMD contribution to taxable income is about \$ 36,500 each year
 - No RMD in 2019 and two in 2020 \rightarrow RMD contribution to taxable income of about \$ 73,000 in 2020
 - Could affect his tax bracket, taxes on Social Security, and other income-sensitive items
 - Deferring the first year RMD may mean more total tax than if the two RMD's were spread over two years.

RMD and Income Taxes

RMD's can push taxpayers into a higher income tax bracket

Example of Fred and Wilma

- After a standard deduction of \$ 26,600., Fred and Wilma have a Taxable Income of \$ 60,000.
- Adding in Fred's RMD of \$ 36,496 brings their Taxable Income to \$ 96,496.

	Income	Tax
Without RMD	\$ 60,000	\$ 6,800
With RMD	\$ 96,496.	\$ 13,104
Tax Increase due to RMD		\$ 6,300
Effective tax rate on RMD		17%

2019 Tax Rates

Rate	For Unmarried Individuals, Taxable Income Over	For Married Individuals Filing Joint Returns, Taxable Income Over
10%	\$0	\$0
12%	\$9,700	\$19,400
22%	\$39,475	\$78,950
24%	\$84,200	\$168,400
32%	\$160,725	\$321,450
35%	\$204,100	\$408,200
37%	\$510,300	\$612,350

- 2018 tax law made these changes effective through 2025
- In 2026 taxes revert to old rates which are 3-4% points higher

RMD's and Social Security

- **Social Security Taxes**
 - The percent of your Social Security Benefit which is taxed depends upon your total income.
 - The tax rate for Social Security increases with your total income.
 - In effect, Social Security benefits are doubly taxed by higher income.
- **Deferring Social Security benefits until age 70**
 - At age 70, additional income from Social Security
 - At age 70 ½, additional income from RMD
 - Both can boost taxable income in same year so need to be considered in tax planning

Combined Income*		Percent of Total Social Security Benefits which are Taxable
Individual	Married Filing Jointly	
\$ 0 to \$25,000	\$ 0 to \$ 32,000	0 %
\$ 25,000 to \$ 34,000	\$ 32,000 to \$ 44,000	Up to 50%
\$ 34,000 +	\$ 44,000 +	Up to 85%
*Combined Income = Adjusted Gross Income (wages, pensions, dividends, and RMD) + Half Social Security Income		

RMD's and Medicare

Medicare Parts B and D Premiums May Increase due to RMD's

Change the facts for Fred and Wilma

- \$ 100,000 taxable income without RMD
- \$ 2,000,000 in IRA
 - \$ 73,000 in first year RMD
- \$ 173,000 of taxable income with RMD
- Medicare monthly premiums for Fred and Wilma:
 - $2 \times \$135. = \$ 270.$ month w/out RMD
 - $2 \times (\$189.60 + \$12.40) = \$ 404.$ month with RMD
- \$ 1,620. annual Medicare premium increase with RMD

Medicare Part B (Hospital) and Part D (Drug) Premiums Are Dependent Upon Yearly Income

If your yearly income in 2017 (for what you pay in 2019) was		Monthly Premiums (in 2019) for Parts B & D
Individual Tax Return	Married Jointly	
\$85,000 or less	\$170,000 or less	\$135.50
above \$85,000 up to \$107,000	above \$170,000 up to \$214,000	\$189.60 + \$12.40
above \$107,000 up to \$133,500	above \$214,000 up to \$267,000	\$270.90 + \$31.90
above \$133,500 up to \$160,000	above \$267,000 up to \$320,000	\$352.20 + \$51.40
above \$160,000 and less than \$500,000	above \$320,000 and less than \$750,000	\$433.40 + \$70.90

Mitigating RMD's – Qualified Charitable Distributions

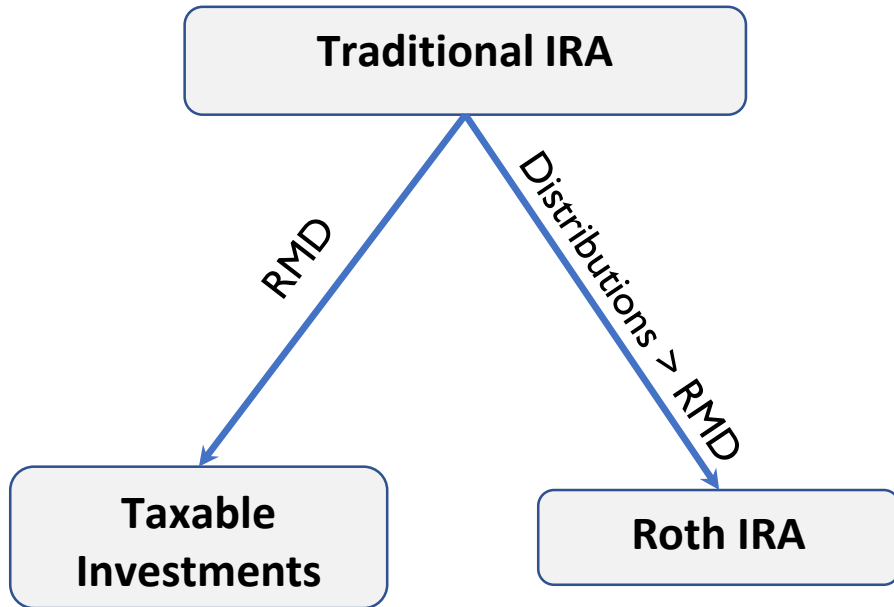
Qualified Charitable Distribution - QCD

- Many married taxpayers subject to RMD's are expected to take the Standard Deduction (\$ 26,600) rather than itemize deductions including charitable contributions. Any charitable contributions may not be deductible.
- The 2018 tax changes allow charitable contributions made directly from an IRA to be included in the RMD but not taxed.
 - The maximum amount of the charitable contribution is limited to the amount distributed from the IRA.
 - The charitable contribution must be made directly from the investment company holding the IRA to the charitable organization. The taxpayer must receive an acknowledgement from the charity for the contribution.
- Example
 - Your required RMD for the year is \$30,000.
 - You instruct the investment company holding the IRA to distribute \$10,000 to the qualified charity.
 - You take an additional \$20,000 distribution from your IRA to satisfy the remaining RMD requirement.
 - On your income tax return:
 - **Income from your IRA:** \$30,000, the total IRA distribution
 - **Taxable amount of IRA income:** \$20,000, the \$10,000 QCD contribution to the charity is not taxable income
 - Your reduction in taxable income is \$10,000. In the 22% tax bracket the tax reduction would be \$2,200, the same as a for a deductible charitable contribution.

Mitigating RMD's – Roth IRA Conversions

- Roth IRA's are IRA's with several differences from traditional IRA's
 - No taxes on increases in the value of investments in Roth IRA's
 - No taxes on withdrawals from Roth IRA's after age 59
 - No requirement to take distributions from Roth IRA's. In particular, no requirement to take distributions at any age.
- Funding Roth IRA's
 - Funds may be **contributed** to Roth IRA's at any age at which you have taxable compensation (e.g. wages, self-employment income)
 - Funds may be **converted** from a traditional IRA to a Roth IRA
 - Amount converted is taxable.
 - Only IRA withdrawals in excess of amount required for RMD can be converted to Roth
 - Funds cannot be withdrawn from Roth until after the 5-year period beginning with the first taxable year for which a contribution was made to the Roth IRA – basically, you must wait 5 years before you can take distributions from the Roth
- An optimum period for conversion of traditional IRA to a Roth IRA is the period between the time when a taxpayer retires (i.e. has reduced earned income) and the time when they turn 70 ½ .
 - With reduced income, their tax rate is lower than before when they were working and when the RMD's begin to add to income
 - The entire amount of the withdrawal from the traditional IRA can be converted into the Roth IRA.

Mitigating RMD's – Asset Allocation



	Taxable	Traditional IRA	Roth IRA
Marginal Tax	22% - 37%	22% - 37%	0% after initial conversion from traditional IRA
Long-term Capital Gains and Stock Dividends	15% - 20%	22% - 37%	0%
Appropriate Types of Assets	<ul style="list-style-type: none"> • Stocks • Stock ETF's • Tax-efficient mutual funds (e.g. index funds) • Muni-bonds 	<ul style="list-style-type: none"> • Taxable bonds and bond funds held for income 	<ul style="list-style-type: none"> • Long-term growth stocks and funds
Assets to be Avoided	<ul style="list-style-type: none"> • Taxable bonds and bond funds 	<ul style="list-style-type: none"> • ETF's and stocks with capital gains • Mutual funds with capital gain distribution 	<ul style="list-style-type: none"> • Slow-growth stocks and funds • Dividends • Bonds

References

- [IRS Pub. 590a](#) - Contributions to Individual Retirement Arrangements (IRAs)
- [IRS Pub. 590b](#) - Distributions from Individual Retirement Arrangements (IRAs)

Comments Questions