DISTRIBUTION PLANNING

In 5 Easy Steps

2.5 Million Baby Boomers Will Turn Age 70 in 2016

Get the Definitive Guide to RMD Planning at: www.irahelp.com/rmd-guide
Calculating the Pro-Rata Rule in 5 Easy Steps

What is the pro-rata rule?
The pro-rata rule is the formula used to determine how much of a distribution is taxable when the account owner holds both after-tax and pre-tax dollars in their IRA(s). For the purposes of the pro-rata rule, the IRS looks at all your SEP, SIMPLE, and Traditional IRAs as if they were one. Even if you have been making after-tax contributions to a separate account for years, and there have been no earnings, you cannot isolate your after-tax amounts and must take your other IRAs into consideration.

1. Total up all of your IRAs. Calculate the total balance of all of your IRAs. Include the balances from each of your IRA accounts, including SEP IRAs and SIMPLE IRAs. Roth IRA balances and balances from any non-IRA based company plans are NOT included for this purpose.

2. Total up all after-tax dollars in IRAs. Calculate the total balance of all after-tax dollars in all of your IRAs. After-tax dollars are either non-deductible contributions made directly to an IRA or rollovers of after-tax dollars from a company plan. If this is not the first year you have had after-tax dollars in your IRA, you should be able to find the previous year’s after-tax total on IRS Form 8606.

3. Calculate your percentage of after-tax dollars. Divide your after-tax IRA dollars (step 2) by your total IRA balance (step 1). If you have $20,000 of after-tax dollars in all your IRAs and the total balance of all your IRAs is $100,000, your percentage of after-tax dollars is 20% ($20,000/$100,000 = 20%).

4. Determine the taxable amount of your distribution. Take the total of all your distribution and multiply it by the percentage you have arrived at in step #3. This is the total amount of the distribution that is tax free. If, in our example, a distribution of $10,000 was made, the tax-free portion would be $2,000 (20% x $10,000 = $2,000). The remaining portion of the distribution ($8,000) would be taxable at ordinary rates.

5. Exception for rollovers to a company plan or charitable rollovers. Under the Tax Code, only pre-tax dollars can be rolled from an IRA into a company plan. If you are making a rollover from your IRA to a company plan, disregard the pro-rata rule altogether. Just be careful not to roll over more than the total amount of pre-tax dollars in your IRA. Qualified charitable distributions (QCDs) from IRAs also disregard the pro-rata rule.
Calculating Your RMD in 5 Easy Steps

What is an RMD (required minimum distribution)?
An RMD is the minimum amount that must be withdrawn from a retirement account each year.

When are you subject to RMDs?
Traditional IRA owners are subject to RMDs beginning in the year in which they turn age 70 ½. Beneficiaries of IRAs and/or Roth IRAs are subject to RMDs beginning in the year after the year of the IRA (or Roth IRA) account owner’s death.

#1 Determine your distribution year. The distribution year is the year for which you are taking a distribution, not necessarily the year in which you take that distribution. For instance, if you turn age 70 ½ in 2016, you do not have to take your first RMD until April 1, 2017. If you wait until April 1, 2017 to take that distribution however, the distribution year is still for 2016. In addition, you will have to take a second distribution by the end of 2017 for 2017. After the year you turn age 70 ½, all distributions should be made by December 31 of each year for which they are being taken.

#2 Find the retirement plan balance. Use the balance as of December 31 of the prior year. Add back any outstanding rollovers and recharacterizations.

#3 Determine the life expectancy factor. Most IRA owners look up their age on the Uniform Lifetime Table in order to determine their factor. If a spouse is the sole beneficiary of an IRA account for the entire year and is more than 10 years younger than the account owner, the Joint Life Expectancy Table is used. Most beneficiaries look up their life expectancy in the year after the year of the account owner's death using the Single Life Table. Going forward each year that factor would simply be reduced by one (there are some exceptions for spousal beneficiaries). Make sure to look up the actual ages of the individual as of the last day of the year.

#4 More mathematics. Divide the retirement plan balance (step 2) by the life expectancy factor (step 3). The result is the RMD that must be taken. Be sure to take the RMD by December 31 of the distribution year (except IRA owners in the year they turn 70 ½). REMEMBER there is a 50% penalty for any portion of an RMD that is not taken.

#5 Take notice. RMDs from owned IRA accounts can be aggregated and RMDs from owned 403(b) accounts can be aggregated. Accounts inherited from the same person can aggregate RMDs. All other types of accounts cannot be aggregated.

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Fixing a Missed RMD in 5 Easy Steps

What is a missed RMD (required minimum distribution)?

RMDs must be taken by IRA owners beginning in the year they turn age 70 ½ and by IRA and non-spouse Roth beneficiaries beginning in the year after the death of the account owner. RMDs not taken are subject to a penalty of 50% of the amount not taken each year.

When should you look for a missed RMD?

You should look for a missed RMD every year after an account owner turns age 70 ½ and when an IRA or non-spouse Roth beneficiary inherits an IRA. Ask your advisor to double check any calculations to be sure they are correct.

Look at the balance sheet. Determine the prior year-end IRA balance for the year that an RMD was not fully satisfied. (Note: There were no IRA RMDs for 2009.)

Determine the life expectancy factor for all missed years. IRA owners use their age each year and look up the corresponding factor on the Uniform Lifetime Table. Non-spouse IRA beneficiaries use their age only in the year after the account owner’s death and look up the corresponding factor on the Single Life Expectancy Table. In each subsequent year, a beneficiary will subtract one from the previous year’s factor. (Remember: These are the general rules for determining life expectancy factors. There are many exceptions to these rules.)

Do some simple math. Divide the account balance by the life expectancy factor for each missed year’s RMD and withdraw that amount from the IRA.

Important forms to file. File IRS Form 5329 for each missed RMD to report the missed distribution and penalty. The penalty can be waived for good cause. Attach a letter to the form requesting a waiver. It is helpful to include language in your letter explaining to the IRS why the distributions were missed, that the problem has been corrected and that procedures are in place to avoid future problems.

It will never happen again. Set up procedures to ensure you take future RMDs. Many custodians offer an option to distribute RMDs automatically each year. If you struggle to remember to take your RMD, setting up an automatic distribution may be beneficial.

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Planning For Multiple Beneficiaries in 5 Easy Steps

When do multiple beneficiaries exist?
Multiple beneficiaries exist when an individual names more than one beneficiary for their IRA.

When should you name more than one beneficiary?
When you want your IRA assets to go to more than one person or entity without having to incur additional fees or paperwork by maintaining separate accounts for each beneficiary.

#1 Due date for designated beneficiaries. September 30 of the year following the year of the IRA owner’s death is the date designated beneficiaries are determined for purposes of post-death stretch payments.

#2 Due date for non-designated beneficiaries. These beneficiaries should be cashed-out before the September 30 date mentioned above. These beneficiaries include charities, estates and non-qualifying trusts since they have no measurable life expectancies. If they are not cashed out in time, they could prevent other beneficiaries from being able to stretch out distributions.

#5 Due date for separate inherited IRAs. These should be established and funded for each designated beneficiary by December 31 of the year following the year of the account owner’s death. These accounts must retain the decedent’s name as part of their title and include language identifying them as “inherited” or “beneficiary” accounts, but they must use the beneficiary’s social security number for reporting purposes.

#4 Maximize the stretch. Each designated beneficiary identified by September 30 can utilize his or her own single life expectancy to maximize the stretch IRA if a separate account is established and funded by December 31. The single life expectancy factor is determined in the year following the year of the account owner’s death. Going forward, the factor is simply reduced by one each year (unless the sole beneficiary is the spouse, in which case he/she re-determines his/her life expectancy each year).

#5 What if you don’t split the account in time? The single life expectancy of the oldest beneficiary must be used to calculate payments to all beneficiaries if separate inherited accounts are not established in time.