



The Downside of IRA Required Minimum Distributions (And How to Avoid It)

Some of the best tools for planning for retirement are pre-tax retirement accounts. Your income goes directly into these funds, without being taxed, and then grows tax deferred for years. You don't have to worry about paying taxes on these accounts until you start withdrawing the money during retirement.

But, all good things must come to an end. So, tax law *requires* that you eventually take income from your IRAs — whether you need it or not. This is known as a required minimum distribution (RMD).

The ABCs of RMDs

R: Required. The tax code requires that you begin taking income from your IRA the year you turn 72.

M: Minimum. There is a minimum amount you must take each year. This amount is calculated based on the balance of your IRA accounts, your age, and the age of your spouse.

D: Distribution. This money must be distributed to the owner, designated beneficiary, or a qualifying charity.

The downside

Perhaps you don't need the income from your IRA. Maybe you're still working at 72. Or, you've retired, but you receive enough from your pension and social security to get by. For you, the IRA distribution mandate may feel like more of a burden than a help. How so?

1. When you take an RMD, you need to pay taxes on the income.
2. Your RMD adds to your adjusted gross income (AGI), so it could push you to a higher tax bracket.
3. If the RMD pushes your AGI above \$85,000 (single) or \$170,000 (married filed jointly), you'll have to pay the high-income surcharge on your Medicare premiums.
4. Your increased AGI could also mean more of your Social Security is taxable. This is determined by your "combined income" or "provisional income." Here's how it's calculated: Compute your AGI without Social Security. Add in any tax-free interest earned, and half of the value of your Social Security benefits. If your provisional income is below \$25,000 (single) or \$32,000 (married filed jointly), you won't owe taxes on your Social Security benefits. If your provisional income falls

between \$25,000-34,000 (single) or \$32,000-44,000 (married filed jointly), up to 50 percent of your Social Security benefits may be taxable. And, if your provisional income is above \$34,000 (single) or \$44,000 (married filed jointly), up to 85 percent of your Social Security benefits may be taxable.

And, you can't skip taking your RMDs. Doing so results in a hefty penalty payable to the IRS – 50 percent of the distribution you don't take in a tax year. So, if your RMD for the year is \$4,000 and you don't take it, you will owe the IRS \$2,000.

How to avoid the tax consequences

The way to avoid this downside of RMDs is to use the distributions for your charitable giving. But, you need to do so carefully. You don't get the full benefits of your charitable donation if you take the RMD as cash and later give it to charity. That's because the RMD would still be included in your AGI. (But, in that case, the donation *would* be tax deductible.)

To make the donation a non-taxable qualified charitable distribution (QCD), your IRA custodian must send the money directly to your parish or nonprofit of choice. Or, if you want to establish a perpetual charitable legacy during your lifetime, you can use QCDs to build a permanent endowment that will support your parish or favorite charity forever. (Unfortunately, at this time, a distribution from your IRA to a donor advised fund is not a qualified charitable distribution.)

And, if you want to do more of your charitable giving from your IRA, you can roll over money from another qualifying account (just not a Roth account). You can transfer up to \$100,000 annually from your IRA to a 501(c)(3) charity – even if that is more than your RMD.

Or, if you need some income, you can take a partial RMD and make the rest a QCD to satisfy your RMD.

Not yet 72? You can begin making qualified charitable deductions from your IRA the year you turn 70½.

Talk to your professional advisor

Your IRA is a flexible tool to leverage in your tax plan. But, there are some important nuances to consider. So, be sure to talk to your professional advisor about your personal situation when making plans.

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