

RETIREMENT PLANNING

As employees retire and rollover their pension benefits to traditional Individual Retirement Accounts (IRAs), it is important to understand the income tax consequences on withdrawals and the required distributions upon reaching age 70-1/2.

I. Withdrawals From Traditional IRAs

Withdrawals from traditional IRAs are taxed as ordinary income (non-deductible contributions are withdrawn tax-free on a pro-rata basis). In addition to income taxes, a 10% early withdrawal penalty is imposed on withdrawals except if:

1. the person is over age 59-1/2, disabled, or deceased.
2. the withdrawals are part of a scheduled series of substantially equal payments made at least annually for a minimum of five years until the person is at least age 59-1/2.
3. the withdrawals are being used for:
 - A. higher education expenses including tuition, books, or room and board by the IRA owner, his or her spouse, children or grandchildren.
 - B. a first time home purchase (\$10,000.00 lifetime maximum) by the IRA owner or immediate family member.
 - C. medical insurance premiums during a period of unemployment in which the person has been receiving federal or state benefits for at least twelve consecutive weeks.
 - D. medical expenses that exceed 7.5% of AGI in any given tax year.

II. Required Distributions

Upon reaching age 70-1/2, an IRA owner must start withdrawing minimum amounts from his/her IRA(s) by December 31 of each year. The first year required distribution may be delayed until April 1 of the year following the year in which the person attains age 70-1/2 (Required Beginning Date). Withdrawals may be from one or more IRAs. However, if sufficient funds are not withdrawn each year, there is a 50% tax penalty on any shortfall.

To calculate a required minimum distribution (RMD), the IRA owner must add the value of all IRAs as of December 31 of the previous year and divide by the appropriate life expectancy factor from the Uniform Table (MDIB) prescribed by the IRS. The exception is for IRA owners who have a spouse beneficiary more than ten years younger - they may use the joint life expectancy table prescribed by the IRS.

III. Death of the IRA Owner

Upon death of the IRA owner, there are several distribution options depending on whether death occurred before or after the Required Beginning Date (RBD) and the status of the beneficiary(ies).

IRA beneficiaries may be changed anytime during the IRA owner's lifetime. At death, the beneficiaries are "locked in". However, some post-death planning may be done during the "gap period" from the date of the IRA owner's death to September 30 of the following year when the "designated" beneficiary is determined. For example, new beneficiaries cannot be added; however, existing beneficiaries may disclaim their interests, or cash-out their shares of the account.

A. Spouse is sole beneficiary (or if multiple beneficiaries and the spouse's share is split into a separate account by 12/31 of the year following the year of death):

1. If the IRA owner died before his/her RBD, the spouse beneficiary may:

- a. withdraw all funds and pay taxes on the distribution.
- b. disclaim in writing, all or a portion of the IRA assets within nine months of date of death.
- c. roll over the assets into his/her own IRA or treat the IRA as his/her own.
- d. establish the IRA as a "decendent/beneficiary IRA" and withdraw funds based on his/her "recalculated" single life expectancy beginning no later than the later of:

December 31 of the year the deceased spouse would have reached age 70-1/2.

December 31 of the year in which the IRA owner died.

- e. withdraw all funds according to the five year rule (all funds must be withdrawn by 12/31 of the fifth year following the year of the IRA owner's death).

2. If the IRA owner died after his/her RBD, the decedent's required minimum distribution must first be withdrawn for the year of death. Then, the spouse beneficiary may:

- a. withdraw all funds and pay taxes on the distribution.
- b. disclaim in writing, all or a portion of the IRA assets within nine months of date of death.
- c. roll over the assets into his/her own IRA or treat the IRA as his/her own.

- d. establish a "decident/beneficiary IRA" and withdraw funds based on a period not longer than the longer of the spouse beneficiary's recalculated single life expectancy or the decedent's remaining term certain life expectancy using the decedent's age in the year of death.

B. Non-spouse Beneficiary(ies)

1. If the IRA owner died before his/her RBD, the non-spouse beneficiary may:

- a. withdraw all funds and pay taxes on the distribution.
- b. disclaim in writing, all or a portion of the IRA assets within nine months of date of death.
- c. withdraw all funds according to the five year rule (all funds must be withdrawn by 12/31 of the fifth year following the year of the IRA owner's death).
- d. establish a "decident/beneficiary IRA" and withdraw funds starting no later than 12/31 of the year following the year of death using the single life term certain method.

If there are multiple beneficiaries, separate beneficiary IRAs should be established by 9/30 of the year following the year of death and the assets should be "split" into those accounts by 12/31. If multiple accounts are not established, the age of the oldest beneficiary is used to determine required withdrawals - even if the IRA is split later on.

If there is no designated beneficiary or the beneficiary is not an individual, all funds must be distributed according to the five year rule. Special distribution rules may apply when a trust is named as beneficiary.

2. If the IRA owner died after his/her RBD, the decedent's required minimum distribution must first be withdrawn for the year of death. Then the non-spouse beneficiary may:

Select option a, b, or d from above; or if the beneficiary was older than the IRA owner, withdraw funds using the single life term certain method based on the decedent's age in the year of death.

If there is no designated beneficiary or the beneficiary is not an individual, funds must be withdrawn using the single life term certain method based on the decedent's age in the year of death (or faster).

The IRS rules on withdrawals from retirement accounts are very complex and this Article is intended to be used only as a quick summary for IRA withdrawals. I strongly recommend that you consult with your financial advisor and/or accountant prior to acting on this information.