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The IRA Digest

Retirement Account Strategies and Tips

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The Top 5 IRA Reminders for Year-End 2022

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Missing the year-end deadline for some IRA transactions could mean missing out on tax saving opportunities or being subject to excise taxes.

If you are one of the 60 million plus individuals with an IRA, you might need to complete certain IRA transactions by the end of this year.

Meeting this deadline could mean taking advantage of tax planning strategies or avoiding IRS-assessed excise tax for the year. The following is a high-level overview of 5 common IRA transactions that are usually required to be completed by the end of the year.

1. RMDs: If You are at Least Age 72 by Year-End

If you own traditional, SEP, or SIMPLE IRAs (traditional IRAs) and you are at least age 72 by December 31 of this year, you must take your required minimum distribution (RMD) from your IRA for the year. Generally, an RMD for an IRA owner must be distributed from the IRA by the end of the year. However, if you turned age 72 this year, you get an extended deadline to April 1 next year to take this year's RMD. This April 1 date (April 1 after the year in which you reach age 72) is your required beginning date (RBD). The RBD is the deadline by which an IRA owner must start taking RMDs.

If You Miss the Deadline

If you miss your RMD deadline, you will owe the IRS an excise tax of 50% of any shortfall. For example, if your RMD is $10,000 and you withdraw only $5,000 by December 31 (April 1 of next year, if you just reached age 72 this year), you will owe the IRS an excise tax of $2,500 (50% of the $5,000 shortfall).

Your RMD Notice

Your IRA custodian must send you an RMD notice by January 31 of any year for which you are supposed to take an RMD. Your RMD notice should include either your calculated RMD amount or an offer to calculate the amount upon request.

Please provide a copy of your RMD notice to your tax advisor, so that they may review any RMD calculation provided by your IRA custodian and make adjustments if necessary.

RMDs do not apply to Roth IRA owners.

2. RMDs: For Some Inherited IRAs

If you inherited an IRA, you might need to take an RMD from that inherited IRA.

Whether you must take an RMD as a beneficiary is determined by multiple factors including your relationship with the IRA owner, whether the IRA was inherited before 2020, and whether the IRA owner died before they were required to start taking their own RMDs.

Beneficiary RMDs apply to both traditional IRAs and Roth IRAs.

Your IRA custodian is not required to calculate your RMD for any inherited IRAs.

If the IRA Owner Died This Year

If the IRA owner died this year and was supposed to take an RMD but did not, you will need to take that RMD. That RMD is calculated as if the owner lived through to the end of the year.

The deadline for taking the RMD, which the owner should have taken, is the end of the year. However, the 50% excise tax is waived if you take it by your tax filing due date for this year, plus extensions.

If the IRA Owner Died before This Year

If the IRA owner died before this year, you are required to take an RMD this year only under the following circumstances.

- **If the 5-year rule applies and the 5-year period ends this year**: The terms of the IRA agreement could require that the 5-year rule apply if the IRA owner died before 2020 and the death occurred before the IRA owner's RBD. Under the 5-year rule, distributions are optional until the end of the 5th year that follows the year in which the IRA owner died, at which time the entire balance must be distributed. 2020 is not counted for this purpose, because RMDs were waived for IRAs for 2020. As a result, the 5-year period would end this year if the IRA was inherited in 2016. In that case, the entire balance that remains at the end of the year would be the RMD.
- **If the life expectancy rule applies**: The life expectancy rule means that distributions must be taken over the beneficiary's life expectancy. Unless the owner dies on or after their RBD and has a life expectancy that is longer than the beneficiary's, in which case the owner's life expectancy would be used to calculate RMDs.

  When the life expectancy rule applies, distributions must begin by December 31 of the year that follows the year in which the IRA owner died and continue for every year thereafter until an end date as required by the governing RMD regulations.

Check with your IRA custodian to determine which RMD rules apply to any IRA that you inherited.

Like IRA owners, beneficiaries will owe the IRS a 50% excise tax on any RMD not taken by the deadline.

3. Qualified Charitable Distributions

If you are at least age 70 ½, you can make a qualified charitable distribution (QCD) from your traditional or Roth IRA- including beneficiary IRAs. A QCD is excluded from your income if it meets certain requirements. These include:

- It must be distributed from your IRA on or after the date that you reach age 70 ½.

- It must be made payable to an eligible charity.
- It must be made from an IRA. Any IRA- including inherited IRAs- qualify unless the IRA is a SEP or SIMPLE IRA that received a SEP or SIMPLE contribution during the year.

A QCD must leave the IRA by December 31 to count for this year.

If you are at least 72, you can use your QCD to satisfy your RMD. For this to work, the QCD must be distributed before other distributions that would satisfy your RMD.

Caution: If you made deductible traditional IRA contributions for the year you reach age 70 ½ or after, let your tax preparer know, as the nontaxable portion of your QCD might need to be reduced by those deductible contributions.

4. SEPP/72(t) Payments: Avoiding the 10% Early Distribution Penalty

Distributions taken from your IRA before you reach age 59 ½ are subject to a 10% additional tax (early distribution penalty) unless you qualify for an exception. One such exception is distributions taken under a substantially equal periodic payment (SEPP) program- commonly referred to as 72(t) payment after the section of the governing tax code.

SEPP/72(t) programs are subject to a strict set of rules, one of which is that any amount for a year under the program must be taken by the end of the year. Failure to take any required amount by the deadline could result in the disqualification of your SEPP program. Any disqualified SEPP program would result in all penalties that were waived under the program being owed to the IRS plus interest.

5. Roth IRA Conversions: Taking Advantage of Tax-Free Growth

Converting assets from a traditional IRA to a Roth IRA would result in any subsequent earnings being tax-free once you are eligible for a qualified distribution. A distribution is qualified if it is taken at least five years after you fund your first Roth IRA, and you are at least age 59 ½ or disabled or withdrawing up to $10,000 for first-time homebuyer purposes. In exchange, income tax on any pre-tax amount included in the conversion must be paid the year the conversion is done, by the tax filing due date.

This tax-free opportunity is a tax-efficient trade-off for paying the income tax now for those for whom a Roth is more suitable than a traditional IRA. Ideally, a suitability assessment should be done to determine if a Roth conversion is a good fit for you.

Assets must leave the traditional IRA by December 31 for the Roth conversion to apply to this year.

Some Financial Institutions Have Earlier Deadlines

While the statutory deadline for these transactions is December 31, some financial institutions have earlier deadlines. These earlier deadlines are established to help ensure that they can handle the influx of requests that are usually submitted as it gets closer to the end of the year. Those with deadlines earlier than December 31st will often guarantee that requests received by a particular deadline will be completed by the end of the year. Requests received after their deadlines are usually completed on a best-efforts basis.

Let Us Help You

The information provided here is merely a high-level overview, and solutions are usually profile-based. What applies to you might be different from what applies to others. If these or any other IRA transactions apply to you, please do not hesitate to contact us for assistance.

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