IRA Masterclass Session 2: Effective Distribution Strategies- From Early Distributions to RMDs

Denise Appleby MJ, CISP, CRC, CRPS, CRSP, APA

Presenter: Denise Appleby

Denise Appleby, MJ, APA, AKS, CISP, CRC, CRPS, CRSP

www.DeniseAppleby.com

Denise Appleby is a nationally recognized author, expert, trainer, speaker, and consultant on IRAs and employer plans for small businesses. She helps financial, tax, and legal professionals avoid mistakes with their clients' retirement accounts and, where possible, fix mistakes.

Due to her knack for helping even the most resistant IRA custodians correct IRA mistakes and resolve other complex IRA-related issues, Denise has earned the reputation of being "The IRA Whisperer".

Denise graduated from John Marshall Law School, where she obtained a Master of Jurisprudence in Employee Benefits and has earned several professional designations for IRAs and employer plans.

Disclaimer & Copyright

This information is for general information purposes only and is not intended to be used as tax or legal advice. You may need additional material to answer some questions related to the course topic.

For legal and compliance reasons, we are unable to answer questions about specific cases, unless we are separately retained for such a consultation.

Learning Objectives

At the end of the session, participants should be able to:

- Identify early distributions and exceptions to the 10% additional tax on early distributions
- Create strategies to retain qualifications for exceptions to the 10% additional tax on early distributions
- Correct IRA Custodian reporting errors
- Managing RMD shortfalls
- Coordinate QCDs with RMDs

Introduction

- Distributions can be taken from IRAs at any time
- A triggering event is required to take distributions from employer plans.
- Distributions are generally treated as ordinary income.
  - Can be taxable or nontaxable.
  - Exceptions apply: Example, net unrealized appreciation (NUA)
- Advisors must know the tax treatment of distributions, tax savings options, and how to avoid penalties.
  - And advise accordingly
- It’s a team effort. The team includes the financial, tax , and (often) legal professionals.

Before you give advice
About a
Distribution/Rollover,
know the risks of moving
forward and plan
accordingly.

Appleby’s Checklist

- The types of accounts on both ends
- The age of the client
- The status of the client: Owner or beneficiary.
- If beneficiary,
  - the class of beneficiary
  - DOB and DOD of participant
- Rollover eligibility of assets
- Whether an employer plan account holds employer securities and/or after-tax amounts.

•Describe the tax impacts of rollovers from employer plans to Roth IRAs

Learning Objective

Identify early distributions and exception to the 10% additional tax

Strategy: Mitigating the 10% additional tax on Early Distributions

www.DeniseAppleby.com

Distributions and the 10% Additional Tax

- When a participant takes a distribution from his/her retirement account, with few exceptions the amount is treated as ordinary income, unless the amount is properly rolled over
- Any taxable portion included in income is subject to a 10% additional tax (early distribution penalty), if the participant was under age 59 ½ at the time of distribution. Exceptions apply!

The Age 59 ½ Factor

Distributions from Retirement Accounts

Age 59 ½ Determination

- Age 59 ½ is reached 6-months after 59th birthday
- Distributions taken before that date is "early distribution" - subject to additional tax, unless exception applies
- Some exceptions apply to IRAs, some apply to employer sponsored retirement plans, some apply to both

Special Rule for SIMPLE IRAs

- The 10% is increased to 25%, if the distribution occurs before the SIMPLE has met the 2-year requirement (the two-year rule)
- The two-year period starts the day the first SIMPLE contribution (employer or employee) is made to the SIMPLE IRA.

No tax
=
no 10%
penalty

Case Study: Amount Subject to the 10% Penalty : Scenario 1

- 40-year-old Andy took a distribution of $80,000 from his traditional IRA
- Andy did not rollover the $80,000 and it was therefore included in his income

Scenario 1: Assume that the entire $80,000 represents pre-tax funds: Andy will owe a 10% additional tax of $8,000 ($80,000 x 10%), unless he qualifies for an exception.

Case Study: Amount Subject to the 10% Penalty : Scenario 2

- 40-year-old Andy took a distribution of $80,000 from his traditional IRA
- Andy did not rollover the $80,000 and it was therefore included in his income

Scenario 2: Assume that $70,000 represents pre-tax funds and $10,000 represents after-tax funds: Andy will owe an additional tax of $7,000 ($70,000 x 10%), unless he qualifies for an exception.

Basis Exception-Traditional IRA

- Nondeductible contributions to traditional IRAs
- Rollover of basis from qualified retirement plans and 403(b)s
- No special reporting on Form 1099-R
- Must file IRS Form 8606 to track basis to avoid double taxation

Distribution of Basis- T-IRA

- Distributions and conversions include pro-rated amount of pre-tax and after-tax (basis) amount
- All traditional, SEP and SIMPLE IRAs aggregated
- Exception to pro-rata rule applies to:
  - Rollovers to employer sponsored retirement plans
  - Qualified charitable distributions
  - Qualified HSA funding Distributions

Reminder

Custodians/Trustees do not withhold the 10% additional tax early distributions

Mitigating the 10% additional Tax

Determine whether the type of account qualifies for an exception

Appleby's 2024 Quick Reference Guide for: Early Distribution Penalty

For Traditional IRAs, Roth IRAs and accounts Under Employer Sponsored Retirement Plans

Use this guide to determine whether a pre- age 59 ½ distribution from an IRA or employer plan account could be exempt from the 10% additional tax (early distribution penalty). Updated with SECURE Act 2.0

Exceptions to the 10% Early Distribution Penalty for IRAs and Other Retirement Accounts

Generally, if you take a distribution from your retirement account before you reach the age of 59½, you will owe the IRS a 10% additional tax (10% early distribution penalty) on the amount. However, there are exceptions to this penalty. The following is a list of these exceptions and the retirement accounts to which they apply.

Exception (Type of Distribution)	Traditional IRA[1]	Roth IRA	Qualified plan, 403(b) and 457(b)[2]
• **Death:** Distributions taken by your beneficiaries after your death	Y	Y	Y
• **Disability:** Distributions taken after you become permanently disabled	Y	Y	Y
• **Basis:** The amount represents basis / after-tax contributions	Y	Y	Y
• **IRS Levy:** The distribution occurs as a result of an IRS levy	Y	Y	Y
• **Rollover:** The amount is rolled over within 60 days of receipt	Y	Y	Y
• **Qualified Reservist:** The amount is a qualified reservist distribution	Y	Y	Y[3]
• **Unreimbursed Medical Expenses:** The amount is used to pay for eligible unreimbursed medical expenses that exceed 7.5% of adjusted gross income	Y	Y	Y
• **SEPP [72(t)] Payments:** Distribution is part of a substantially equal periodic payment (SEPP), commonly referred to as 72(t) payments	Y	Y	Y
• **First-time Homebuyer:** Distribution used to buy, build or rebuild a first home for you or an eligible family member	Y	Y	N
• **Higher Education Expenses:** Used for qualified higher education expenses at an eligible educational institution for you or an eligible family member	Y	Y	N
• **Roth Conversion/Rollover:** Amount converted or rolled over to a Roth IRA	Y	N/A	Y
• **Conversion aged five years in the account:** The amount has been in a Roth IRA for at least five years, after being converted or rolled over.	N/A	Y	N/A
• **Qualified Distribution:** Distribution from a Roth IRA or designated Roth Account [E.g. Roth 401(k)] that meets the requirements to be 'qualified'	N/A	Y	Y[4]
• **Health Insurance Premiums:** Amount used to pay for health insurance premiums for yourself, your spouse, and your dependents; and you receive the distributions during the year you received unemployment compensation or the following year, but no later than 60 days after you have been reemployed	Y	Y	N
• **Qualified birth or adoption distribution distributions:** Up to $5,000, made during the 1-year period beginning on the birth date or on which the legal adoption by the individual of an eligible adoptee is finalized.	Y	Y	Y
• **QDRO:** The amount was distributed to an alternate payee, under a qualified domestic relations order (QDRO)	N	N	Y
• **Age 55:** Distribution taken after you separate from service with the employer that sponsors the plan; separation must occur in the year you reach age 55 or later. Reduced to age 50 or at least 25 years of service for a qualified public safety employee (QPSE) [5]	N	N	Y

New Exceptions Under SECURE Act 2.0

Effective for distributions made after SECURE Act 2.0 date of enactment

- **Terminal illness:** Distributions made by individuals who have been certified by a physician as having an illness or physical condition that can reasonably be expected to result in death within 84 months or less after the certification date. **IRAs and Employer Plans**

New Exceptions Under SECURE Act 2.0

Effective for distributions made after SECURE Act 2.0 date of enactment

- **Corrective distributions of excess contributions**: Any attributable earnings must be included in a correction (return of excess contribution) that is done by the IRA owner’s tax filing due date, plus extensions

New Exceptions Under SECURE Act 2.0

Effective for distributions made after SECURE Act 2.0 date of enactment

- **Domestic Abuse Victims**: **$10,000 for victims of domestic abuse:**
- Victims of domestic abuse may withdraw up to the lesser of $10,000 (adjusted for cost-of-living increase) or 50% of their vested account balance
- during the one-year period that begins on the date of the domestic abuse committed by a spouse or domestic partner.

Effective distributions made after Dec. 31, 2023.

IRAs and Employer Plans

Check State Law

Some states allow a deduction for the 10% additional tax on early distribution

Taxpayers should consult with a CPA regarding deductibility at the state level

IRS Memorandum 20072201F

Get a win for clients: Cautiously Move Between Plan Types

- Be cautions about losing exception by changing plan types.
- Change plan types to gain qualification for exceptions

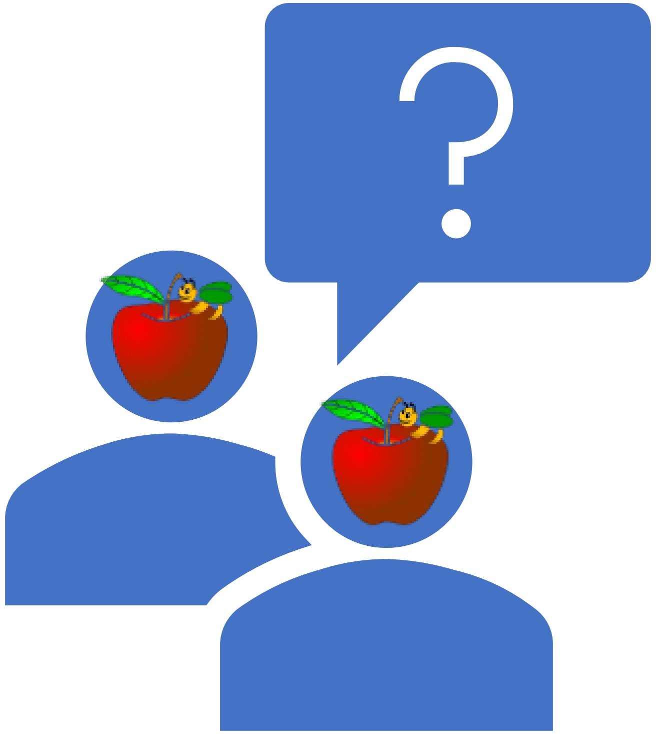
Will exception be lost or gained as a result of change of plan type?

Appleby's 2024 Quick Reference Guide for: Early Distribution Penalty
For Traditional IRAs, Roth IRAs and accounts Under Employer Sponsored Retirement Plans
Use this guide to determine whether a pre- age 59 ½ distribution from an IRA or employer plan account could be exempt from the 10% additional tax (early distribution penalty). Updated with SECURE Act 2.0

Exceptions to the 10% Early Distribution Penalty for IRAs and Other Retirement Accounts

Generally, if you take a distribution from your retirement account before you reach the age of 59½, you will owe the IRS a 10% additional tax (10% early distribution penalty) on the amount. However, there are exceptions to this penalty. The following is a list of these exceptions and the retirement accounts to which they apply.

Exception (Type of Distribution)	Traditional IRA[1]	Roth IRA	Qualified plan, 403(b) and 457(b)[2]
• **Death:** Distributions taken by your beneficiaries after your death	Y	Y	Y
• **Disability:** Distributions taken after you become permanently disabled	Y	Y	Y
• **Basis:** The amount represents basis / after-tax contributions	Y	Y	Y
• **IRS Levy:** The distribution occurs as a result of an IRS levy	Y	Y	Y
• **Rollover:** The amount is rolled over within 60 days of receipt	Y	Y	Y
• **Qualified Reservist:** The amount is a qualified reservist distribution	Y	Y	Y[3]
• **Unreimbursed Medical Expenses:** The amount is used to pay for eligible unreimbursed medical expenses that exceed 7.5% of adjusted gross income	Y	Y	Y
• **SEPP [72(t)] Payments:** Distribution is part of a substantially equal periodic payment (SEPP), commonly referred to as 72(t) payments	Y	Y	Y
• **First-time Homebuyer:** Distribution used to buy, build or rebuild a first home for you or an eligible family member	Y	Y	N
• **Higher Education Expenses:** Used for qualified higher education expenses at an eligible educational institution for you or an eligible family member	Y	Y	N
• **Roth Conversion/Rollover:** Amount converted or rolled over to a Roth IRA	Y	N/A	Y
• **Conversion aged five years in the account:** The amount has been in a Roth IRA for at least five years, after being converted or rolled over.	N/A	Y	N/A
• **Qualified Distribution:** Distribution from a Roth IRA or designated Roth Account [E.g. Roth 401(k)] that meets the requirements to be 'qualified'	N/A	Y	Y[4]
• **Health Insurance Premiums:** Amount used to pay for health insurance premiums for yourself, your spouse, and your dependents; and you receive the distributions during the year you received unemployment compensation or the following year, but no later than 60 days after you have been reemployed	Y	Y	N
• **Qualified birth or adoption distribution distributions:** Up to $5,000, made during the 1-year period beginning on the birth date or on which the legal adoption by the individual of an eligible adoptee is finalized.	Y	Y	Y
• **QDRO:** The amount was distributed to an alternate payee, under a qualified domestic relations order (QDRO)	N	N	Y
• **Age 55:** Distribution taken after you separate from service with the employer that sponsors the plan; separation must occur in the year you reach age 55 or later. Reduced to age 50 or at least 25 years of service for a qualified public safety employee (QPSE) [5]	N	N	Y



Make sure client qualifies for exceptions

Example: First-time Homebuyer: Use of Funds

- Must be used to pay qualified acquisition costs

- Must be used to pay qualified acquisition costs for the main home of a first-time homebuyer, which covers:
  - Owner
  - Spouse
  - Spouse's child
  - Spouse's grandchild
  - Spouse's parent or other ancestor

First-time Homebuyer: Who qualifies

- Who is a first-time buyer:
  - Had no present interest in a main home during the 2-year period ending on the date of acquisition of the home which the distribution is being used to buy, build, or rebuild
  - If married, spouse must also meet this no-ownership requirement

Bonus Tip: First-time Homebuyer: Rollover Deadline

- 60-day extend to 120 days if received a distribution to buy, build, or rebuild a first home and the purchase or construction was canceled or delayed

Expenses Must Occur During Distribution year

IRS Publication 590-B provides details on exceptions

33

457(b) Special Rule

- Pre-tax amount is ordinary income
- No additional tax on early distributions. Exception applies to amounts rolled over from other plans

Death Exception-Caution

- Death distributions exempt from the 10% additional tax on early distributions
  - Code 4 in Box 7 of Form 1099-R
- Spouse beneficiary can treat as own or as inherited IRA
- If under age 59 ½ , 10% additional tax applies if spouse treats as own
- Spouse can change from inherited IRA at any time

Real Life Case!

Spouse Beneficiary Loses Death Exception

The Case: Peggy Ann Sears v. Commissioner, T.C. Memo. 2010-146

Confusion: Whether Death Penalty exception applies when "spouse treats as own"

- The individual inherited her husband's IRA. Transferred to her "own" IRA.
- She made withdrawals from the IRA while she was under age 59 ½, but did not pay the penalty
- The IRS amended her tax return to assess the 10% additional tax on early distribution: $6,093.70
- The tax court agreed

Disability Exception

- An individual shall be considered to be disabled if unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or to be of long-continued and indefinite duration
- Proof of disability required – Chief Counsel Advice 200922041
- A medical determination must be made
- Code 3 in Box 7 of Form 1099-R

Real Life Case!

Disability Exception

Dollander v. Commissioner- T.C. Memo. 2009–187 (Aug. 19, 2009)

- Nurse diagnosed with post-traumatic stress disorder and depression
- Restricted to light duty, and reassigned to desk
- Not institutionalized or under constant supervision and maintained side business

Assessment: Deficiency in income tax of $16,918 , accuracy-related penalty of $3,384, 10% additional tax on early distribution of $158,310.42

Disability Exception

- Qualifying for disability under private disability insurance contract not sufficient, as different criteria may apply
  - Stipe v. Commissioner, T.C. Memo. 2011-92
  - Kowsh v. Commissioner, T.C. Memo. 2008-204
- Disability must precede distribution
- Requirement met if SSA application for disability is submitted before distribution, and application is approved
- Dart v. Commissioner, T.C. Summary Opinion 2008–158 (T.C. 2008)

•Describe the tax impacts of rollovers from employer plans to Roth IRAs

Learning Objective

Create strategies to retain qualifications for exceptions to the 10% additional tax on early distributions

Strategy: Mitigating the taxability of distributions

www.DeniseAppleby.com

Substantially equal periodic payments

Pre-SEPP

- Check for Other Exceptions before starting a SEPP
- Avoid using for short-term needs

SEPP [72(t)] Payments

- Must meet IRS Safe harbor requirements
- Retroactive 10% additional tax on early distributions, plus interest, if modified
- Continue for 5 years or until 59 ½, whichever is longer
- Must be separated from service for employer sponsored retirement plan

SEPP [72(t)] Payments

Three methods to calculate amount:

- RMD method
- Annuitization method
- Amortization method

A One-Time Switch is Permitted in One Direction

Switching Option

Amortization | Annuitization

RMD

SEPP [72(t)] Payments

- Life expectancy tables
  - Single life expectancy table
  - Uniform lifetime table
  - Joint life expectancy table – must be actual beneficiary
- Age at end of year is used

SEPP [72(t)] Payments: Interest Rate

- For the fixed amortization method and the fixed annuitization method, the interest rate is capped at the greater of:
  - (i) 5%, or
  - (ii) 120% of the federal mid-term rate for either of the two months immediately preceding the month in which the distribution begins.
- The IRS publishes the monthly Applicable Federal Rates (AFRs) here https://apps.irs.gov/app/picklist/list/federalRates.html .
- Use rate for either of the two months immediately preceding the month in which the distribution begins

SEPP [72(t)] Payments

Account balance

- Account balance must be based on reasonable facts and circumstances
- No additional except for gains and losses
- ~~No nontaxable transfer of a portion of the account balance to another retirement plan~~ (restriction repealed under SECURE Act 2.0)

Strategy: Run Calculation Using All Three Methods

- Choose the one that best suits your client
- Use different interest rates
- Use different life expectancy tables.
- Run reverse calculations

SEPP/72(t) Case Study

Starting Date:		**9/2024**
2024 Plan Balance:		$100,000.00
Expected Plan Growth:		5.00%
Distributions Occur Annually		
Owner's Birth Date:		1/1/1975
"Reasonable" Interest Rate:		5.40%

Amortization Method

Date	Age	Balance	Factor	Distribution
9/2024	49	$100,000.00	16.2284	$6,162.04
9/2025	50	$98,529.86	16.2284	$6,162.04
9/2026	51	$96,986.21	16.2284	$6,162.04
9/2027	52	$95,365.38	16.2284	$6,162.04
9/2028	53	$93,663.51	16.2284	$6,162.04
9/2029	54	$91,876.54	16.2284	$6,162.04
9/2030	55	$90,000.23	16.2284	$6,162.04
9/2031	56	$88,030.10	16.2284	$6,162.04
9/2032	57	$85,961.46	16.2284	$6,162.04
9/2033	58	$83,789.39	16.2284	$6,162.04

Compare All Three Methods. Choose one

Year	RMD Method (Amount will change each year) Distribution	Amortization Method Distribution	Annuitization Method Distribution
2024	$2,695.42	$6,294.49	$6,162.04
2025	$2,822.37	$6,294.49	$6,162.04
2026	$2,955.09	$6,294.49	$6,162.04
2027	$3,102.85	$6,294.49	$6,162.04
2028	$3,248.24	$6,294.49	$6,162.04
2029	$3,400.15	$6,294.49	$6,162.04
2030	$3,558.86	$6,294.49	$6,162.04
2031	$3,736.81	$6,294.49	$6,162.04
2032	$3,897.31	$6,294.49	$6,162.04
2033	$4,078.02	$6,294.49	$6,162.04
Total:	$33,495.12	$62,944.90	$61,620.40

SEPP [72(t)] Payments

Changes allowed

- Complete depletion of balance, SEPP terminated
- One time change to RMD method
- Death
- Disability

There is a Recapture Tax for Breaking the Rules

Fastest Way to determine the taxability of a Roth IRA distribution

Check if Distribution is qualified

1. Had client funded any Roth IRA for 5-years? **and**
2. Is any of the following an applicable event?
   a. Age 59 ½ older
   b. Death
   c. Disability
   d. Up to $10,000 first time home

If yes, stop! Distribution is tax-free and penalty free.

If no (next slide)

Apply the Ordering Rules for Nonqualified Distributions From Roth IRAs

Contributions, DRA Basis, 529 Basis 1st

Never get to next tranche until these amounts are fully distributed

Withdraw anytime as needed

Conversions and Rollovers 2nd FIFO

Never get to next tranche until these amounts are fully distributed

Wait 5-years : F.I.F.O. or when other exception applies

Earnings 3rd (last)

Never get to this tranche until other amounts are fully distributed

Wait until distribution is qualified.

Summary: Tax Treatment of Roth IRA Distributions

Tax and Penalty Treatment of Roth IRA Distributions		
Source of distributed assets (Ordering rules)	**Qualified Distributions**	**Non-qualified Distributions**
• Contributions and rollover of basis from DRA and 529 plans: distributions come from this source first	• Tax Free • Penalty Free	• Tax Free • Penalty Free
• Conversions and rollovers: distributions come from this source second on a first in first out (FIFO) basis	• Tax Free • Penalty Free	• Tax Free • 10% penalty applies <u>if</u> no exception
• Earnings: distributions come from this source last	• Tax Free • Penalty Free	• Tax applies • 10% penalty applies <u>if</u> no exception

•Describe the tax impacts of rollovers from employer plans to Roth IRAs

Learning Objective

Managing RMD Shortfalls

New RMD Ages

Year/date of birth	Applicable age for IRA Owners: When RMDs begin
June 30, 1949, and earlier	The year they attained age 70½
July 1, 1949–December 31, 1950	The year they attained age 72
January 1, 1951–December 31, 1958	The year they attain age 73
January 1, 1959–December 31, 1959	The year they attain age 73*
January 1, 1960, and after	The year they attain age 75
The First RMD must be taken by April 1 of the year after the Applicable RMD Age. * SECURE Act 2 proposed regulations	

What is an RMD?

Required Minimum Distribution (RMD)

- Minimum amount that must be withdrawn from a retirement account for a year
- RMDs start the year the account owner/participant reaches their applicable age (first RMD year)
- Employer plans may allow eligible participants to defer RMDs past their applicable RMD age until retirement
- The RMD amount for a year must generally be withdrawn from an IRA or employer plan by December 31 of the year it is due.

The RMD Formula

- Divide FMV by applicable life-expectancy
- To determine life expectancy:
- Use **Uniform Lifetime table** with one exception
- **Exception: Joint Life and Last Survivor Expectancy table** can be used under exception:
  - ✓ Exception applies where spouse is **(a)** sole primary beneficiary and **(b)** more than 10 years younger than owner
- Use age as of end of RMD year
- For beneficiary accounts: Single Life Expectancy Table

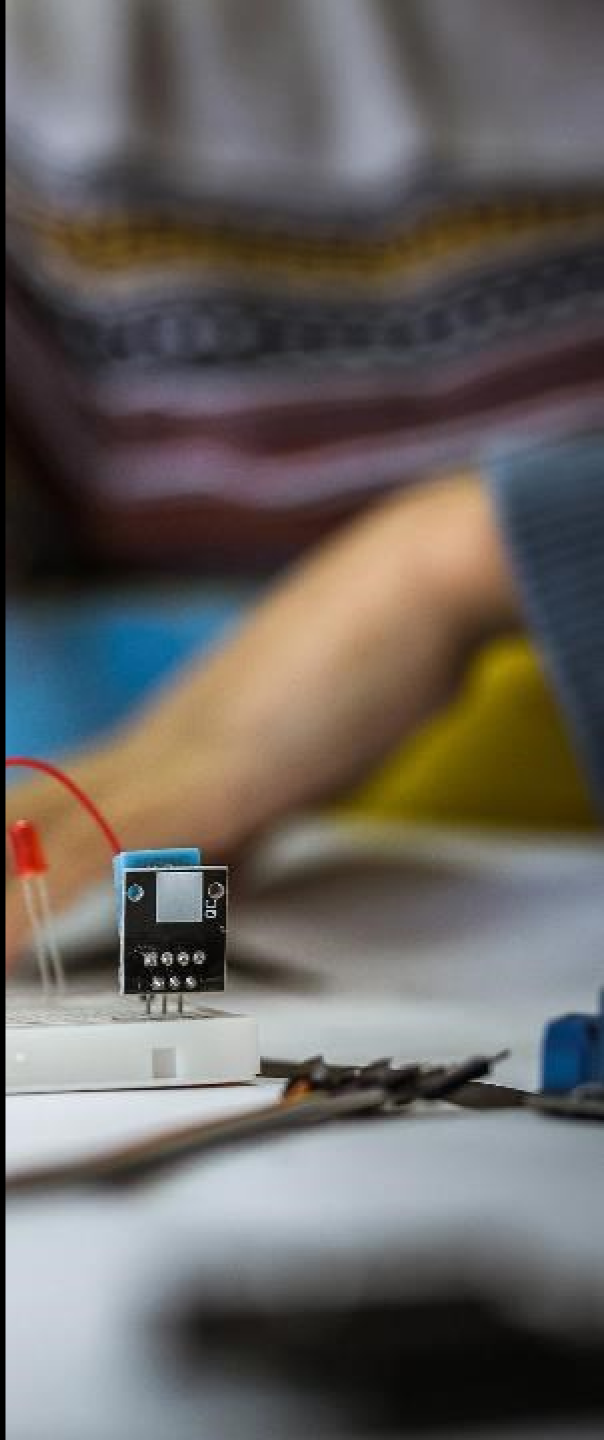
What Is the Required Beginning Date?

- RBD= April 1 of the year that follows the year the account owner reaches their applicable age
- An employer plan may design the RBD as the later of: **(A)** the above or **(B)** April 1 of the year that follows the year the participant retires from the employer
- For **participants** in qualified plans, 403(b)s, and governmental 457(b) plans who can defer RMD past their applicable RMD age until retirement, the first RMD can be deferred until April 1 of the year after year of retirement (RBD)

Consequences of Missing RMD Deadline

- If an RMD amount is not taken by the deadline, an excise tax on the shortfall is owed to the IRS
    - 50% before 2023
    - 25% as of 2023
    - Reduced to 10% if corrected timely
- Applies to account owners and beneficiaries with inherited accounts

Taking the path to correction can reduce the excise tax on RMD failures

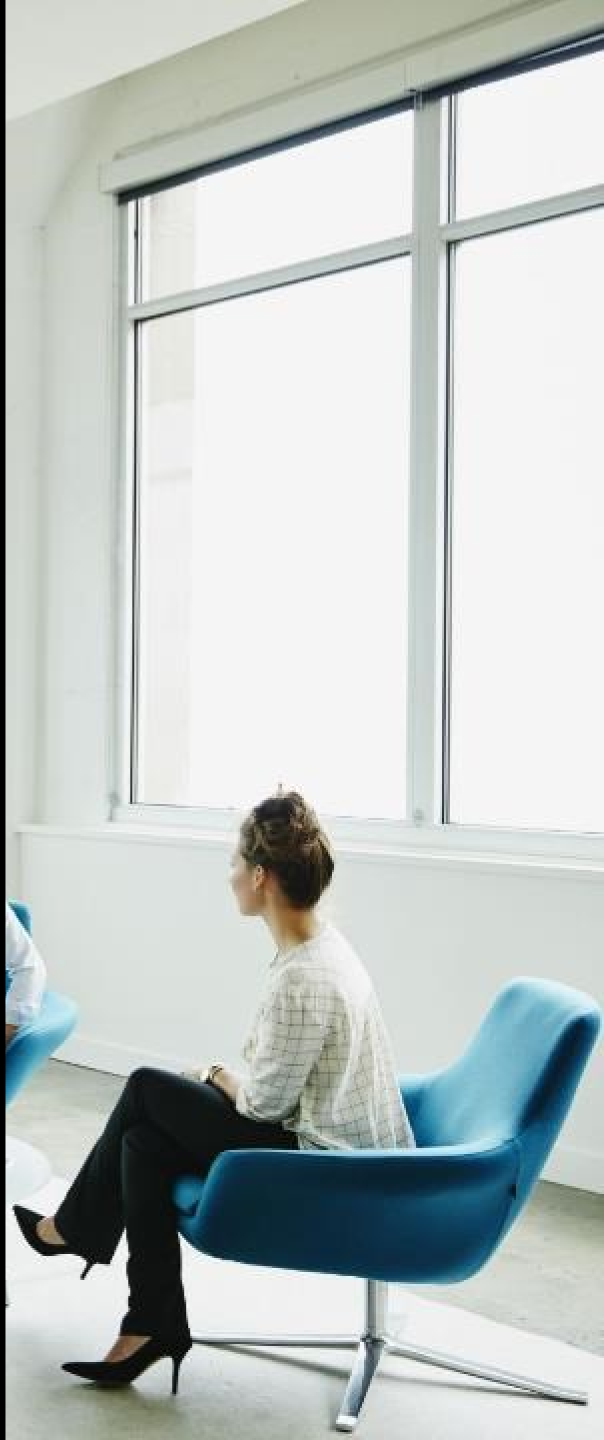


Excise Tax? Request A Waiver

- The IRS may waive the penalty if the failure to meet the deadline was due to reasonable cause
- Form 5329 is used to report penalty
- Penalty must not be paid if waiver is requested unless IRS responds with a denial
- Should take RMD or show attempt to correct shortfall

RMD is a team project. But IRA owners are responsible for paying excise tax on failures.

www.DeniseAppleby.com



•Describe the tax impacts of rollovers from employer plans to Roth IRAs

Learning Objective

Coordinate QCDs with RMDs

Qualified Charitable Distributions

- Qualified charitable distributions (QCDs) are tax-free
- A QCD:
  - Must be distributed on or after the day the IRA owner reaches age 70½
  - Can be made only from traditional IRAs, Roth IRAs, and SEP/SIMPLE IRAs that are not ongoing
  - Must be made to charitable organizations described in Code §170(b)(1)(A)
  - Is limited to $100,000 (indexed) per year per IRA owner.

Source: Appleby's IRA Quick Reference Guides Book www.IRAPublications.com

New RMD Age has no effect on QCDs

www.DeniseAppleby.com

Reminder: Deductible IRA Contributions

- Age repeal of QCD (SECURE Act 1)
- Deductible IRA contribution and QCD can be made at the same time.
- Deductible IRA contribution after age 70 ½ must be coordinated with QCD.

Example 1: QCD Coordination

Example

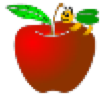
71-year-old Tom:

- Made a 2024 deductible Traditional IRA contribution of $6,000, and
- Made a QCD of $50,000 for 2024
- $44,000 will be tax-free
- $6,000 will be included in his income

Example 2: QCD Coordination

	Deductible IRA contribution	QCD	Excludible Amount	Comment
2022	$5,000	$-0-	N/A	N/A
2023	$5,000	$6,000	$6,000 reduced by $10,000 ($5,000 for 2021 and $5,000 for 2022)	There is no excludible amount $4,000 remains by which to reduce a QCD
2024	$-0-	$6,500	$6,500 reduced by $4,000	The excludible amount is $2,500 ($6,000 -$4,000)

Taking QCDs before RMDs means QCD ≈ RMD



A QCD Can Be an RMD

- A QCD counts as RMD, if done before RMD is satisfied

QCDs as RMD: Case Study 1

- A QCD can be used to satisfy an RMD
- To be an RMD, a QCD cannot be made after RMD has been satisfied

Case study #1: 75-year-old Charlie's RMD for this year is $30,000

- Charlie makes a QCD of $30,000 in January of this year
- The $30,000 is nontaxable because it is a QCD
- The $30,000 counts as Charlie's RMD for this year **because it is her first distribution for the year**
- No additional distribution is required to satisfy Charlie's RMD

QCDs as RMD: Case Study 2

Case study #2: 74-year-old Winsome's RMD for this year is $10,000

- **1.** Suzie takes a distribution of $10,000 in January of this year, and has the amount paid to her
  - Because that is her first distribution this year, it is her RMD for the year
  - It is taxable*, because it is not a QCD
- **2.** Suzie makes a QCD of $5,000 in February
  - The $5,000 is <u>non</u>taxable because it is a QCD

*Except for any basis amounts

•Describe the tax impacts of rollovers from employer plans to Roth IRAs

Learning Objective

Correct IRA Custodian reporting errors

Reminder: IRA Custodians Do Not Track Basis

- All early and normal distributions are reported as taxable
- If any portion is nontaxable, that must be claimed on the IRA owner’s tax return
- To allow for IRA owner’s claim, the IRA custodian must check the “Taxable Amount Not Determined” Box (Box 2b)

PAYER'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone no.

1 Gross distribution
$

2a Taxable amount
$

OMB No. 1545-0119

2024

Form **1099-R**

Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.

2b Taxable amount not determined ☐ Total distribution ☐

Copy A For Internal Revenue Service Center

File with Form 1096.

PAYER'S TIN	RECIPIENT'S TIN	3 Capital gain (included in box 2a) $	4 Federal income tax withheld $
RECIPIENT'S name		5 Employee contributions/ Designated Roth contributions or insurance premiums $	6 Net unrealized appreciation in employer's securities $
Street address (including apt. no.)		7 Distribution code(s) — IRA/ SEP/ SIMPLE ☐	8 Other $ %
City or town, state or province, country, and ZIP or foreign postal code		9a Your percentage of total distribution %	9b Total employee contributions $

For Privacy Act and Paperwork Reduction Act Notice, see the **2024 General Instructions for Certain Information Returns.**

10 Amount allocable to IRR within 5 years $	11 1st year of desig. Roth contrib.	12 FATCA filing requirement ☐	14 State tax withheld $ $	15 State/Payer's state no.	16 State distribution $ $
Account number (see instructions)		13 Date of	17 Local tax withheld	18 Name of locality	19 Local distribution

File Form 8606 to Report Nontaxable Amount

- Rectifies “Taxable amount not determined” Box on 1099-R , if any portion is nontaxable.
- Form 8606 tracks basis.
- Reports deductible IRA contributions.
- Tracks how much of basis is included in a distribution.
- Prevents double taxation.

Custodian Tax Reporting

Exception Codes for Amounts That Might be Included in Income

1099-R and Reporting the Exception

- IRA custodians & trustees (custodians) must issue IRS Form 1099-R for distributions
- Form 1099-R must report some exceptions
- Some exceptions are not reported by custodians

Exception Code Custodian Reporting

- 2—Early distribution, exception applies. Examples include:-
  - Direct Roth conversion
  - Age 55 exception
- 3—Disability.
- 4—Death.

No Exception Reporting by Custodian: 1 of 2

Custodian must use Code 1 even if the distribution is made for medical expenses,

- health insurance premiums,
- qualified higher education expenses,
- a first-time home purchase,
- a qualified reservist distribution,
- a qualified birth or adoption distribution

No Exception Reporting by Custodian: 2 of 2

Custodian must use Code 1 even if the distribution is made for medical expenses,

- an emergency personal expense distribution,
- a terminally ill individual distribution,
- or an eligible distribution to a domestic abuse victim
- if a taxpayer is 59½ or older and they modify a series of substantially equal periodic payments under section prior to the end of the 5-year period that began with the first payment.

Form 5329 Used to Override Code 1

- One of the purposes of Form 5329 is to override or correct the early distribution or exception Code in Box 7 of Form 1099-R

Tips for Advisors

- Inform clients about penalty- avoid sticker shock
- Determine if benefits will be lost as a result of rollover
- Check for penalty exceptions that may not apply to receiving plan
- If custodian does not report exception, file Form 5329 to override custodians reporting
- Check for RMD shortfalls and take steps to avoid the excise tax.
- Coordinate RMDs with QCDs if that is the client’s intent.

Questions?

Send them to Training@DeniseAppleby.com

Thank you for your attention and your time!