

Make the Most of Your RMDs

New rules mean new strategies for distributions from your retirement plan.

For many retirees, a key source of income is the distributions they receive from retirement accounts such as 401(k)s and IRAs. Given that these are fairly heavily regulated and that the rules around them have changed recently, it's worth building a strategy around taking them so you can help ensure your financial needs will be met throughout your retirement. If you're nearing retirement and starting to set up plans for what to do with your retirement accounts, here are some key questions to keep in mind:

WHEN DO I HAVE TO START TAKING MY RMDs?

The SECURE Act, passed toward the end of 2019, updated some of the rules around RMDs. Most notably, for those who haven't retired yet, the law raised the beginning date for taking RMDs from age 70½ to 72 – specifically, by

April 1 of the year after you turn 72. This change gives you the chance to let your assets keep on growing a little bit longer before you have to start drawing them down, a small but potentially significant difference.

There's a way you may be able to wait till even later to take your RMDs: Keep working past the age of 70, and continue contributing to your employer's retirement plan. As long as you don't own more than 5% of the company you work for, you can wait to take your RMDs from that employer's plan until after you've retired.

WHAT DIFFERENCE DOES IT MAKE WHEN I TAKE MY FIRST RMD?

The strategy around taking your RMDs is based to a great extent on what your other income is. You'll want to try to ►

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lower or increase your RMDs in specific years so that they will leave you with the best possible tax situation.

For example, you can delay your first withdrawal until the calendar year after you turn 72. But this may cause you to take two withdrawals in a single year, and the increased income could push you into a higher tax bracket. In addition to raising your tax bill for the year, this could also subject you to increased Medicare premiums. Your Baird Financial Advisor team can help you sort out the tactics and timing that work best for you.

HOW DOES THE IRS DETERMINE WHAT MY RMDs WILL BE?

The IRS uses life expectancy tables to determine RMDs, projecting how your retirement savings are expected to last over the remaining course of your life. The agency issued new tables at the end of 2020, to take effect in 2022. The changes to the life expectancy tables reflect increasing life spans, and allow retirees to take smaller RMDs, thereby allowing more of your assets to continue to grow.

IF I PASS AWAY BEFORE I RETIRE, WHEN DO MY BENEFICIARIES HAVE TO START TAKING THEIR RMDs?

Beneficiaries must begin taking distributions by December 31 of the year following the year of the account owner's death. The amount they have to take is based on the beneficiary's age at that point in time. Eligible designated beneficiaries (EDBs) should use the IRS's Single Life Table to determine their RMDs, which will be based on the beneficiary's own life expectancy. EDBs include spouses (who choose not to roll over or take as their own), disabled or chronically ill individuals, minor children and any beneficiary that is not more than 10 years younger than the owner. If your beneficiaries are not EDBs, they are limited to taking the necessary withdrawals over the ensuing 10 years.

IF I USE MY RMD TO MAKE A CHARITABLE CONTRIBUTION, CAN I AVOID TAXES ON IT?

A distribution from an IRA that is donated directly to a charity, called a Qualified Charitable Distribution (QCD), will not be taxed as income. Through a QCD, you can transfer up to \$100,000 each year directly from an IRA (although not from a 401(k) or other employer-sponsored plan) to an

eligible charity. While this avoids income tax on the RMD, note that QCDs are not eligible to claim as a tax deduction. Please note that unlike with RMDs, the age limit has not changed for QCDs and remains at age 70½.

IS THERE ANY WAY I CAN KEEP THE ASSETS BUT AVOID THE RMDs ALTOGETHER?

You may be able to convert your retirement vehicle into a Roth IRA, which has no RMDs. You will have to pay taxes on the amount that is rolled over, though, and if you're already 72, you must take the RMD before converting. This is only an option if you're converting from a Roth 401(k) or traditional IRA.

Each of these tactics can be complicated to implement. To make sure your retirement plan is still on the right track, check with your Baird Financial Advisor team.

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Please reach out if you or anyone you know would benefit from discussing this topic further.