Paul Winter

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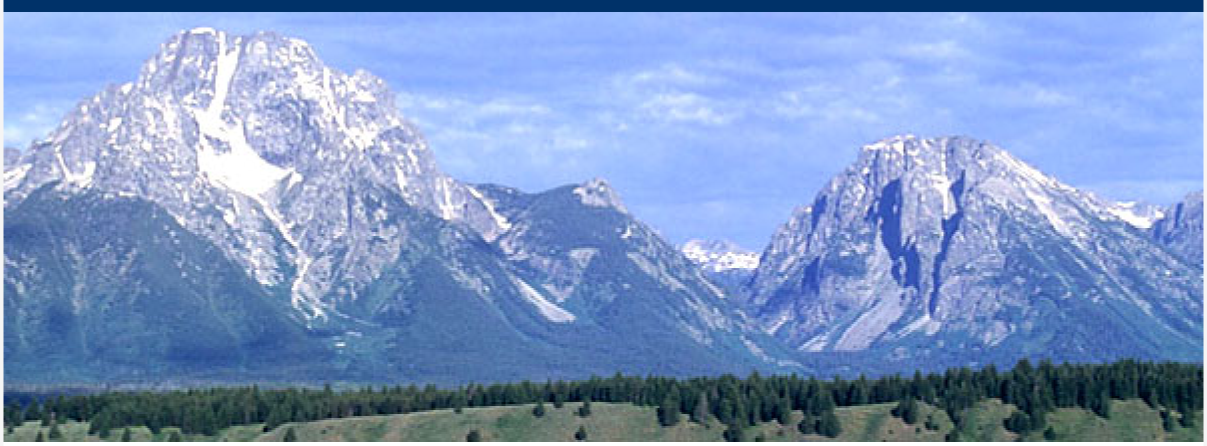
Five Seasons Financial Planning
Guiding You to a Brighter Financial Future

Seasonal Musings Summer 2020



The CARES Act and Required Minimum Distributions

As mentioned in the **prior issue of "Seasonal Musings"**, the passing of the SECURE Act late last year permanently changed the financial planning landscape, and in particular, many of the rules on required distributions from IRA's and retirement plan accounts. The Coronavirus Aid, Relief and Economic Security (CARES) Act, passed just a few months later, contains a number of measures related to the taking of RMD's in this calendar year alone.

First and foremost, all 2020 required minimum distributions have been waived. This provision includes RMD's from IRA's, from retirement plan accounts (like 401k's, 403b's and **457's**), as well as from both traditional and Roth inherited IRA accounts. The waiver also applies to owners of tax-qualified accounts who waited until 2020 to take advantage of the 3-month grace period on their inaugural RMD's for 2019.

It's important to note that the CARES Act results in a permanent avoidance of required distributions for 2020 - as well as the deferral of any related tax bills - and not simply a postponement of them until next year. The Act was signed into law on March 27, near the very lows of this year's stock market crash, and was intended at the time to keep retirees from having to take outsized distributions from depressed account values. (A similar law was enacted for 2009 RMD's for the same reasons during the Great Recession). Ironically, many retirement accounts have now rebounded back to their 2019 year-end values on which the 2020 RMD calculation is based.

What if I've Already Taken My 2020 RMD and Wish I Hadn't?

A recent survey by MagnifyMoney found that 30% of all retirement account owners took distributions from these accounts during a tumultuous 2-month period earlier this year, but that 60% of these investors regret having done so. If you took an RMD earlier this year, either before the passing of the CARES Act or after, and now wish you hadn't, relief is available - but not for long.

Retirees and owners of inherited retirement accounts have the option to rollover any of these regrettable 2020 RMD's until the end of this month, and in the process, to defer any of the tax consequences that would otherwise result from these distributions. Unlike other rollovers from tax-qualified accounts, there is no 60-day deadline associated with these rollovers of RMD's, simply one that dictates that the funds must be replaced by August 31 regardless of when the funds were distributed in 2020. And usually there is only one 60-day rollover permitted in any one-year period, but these RMD rollovers will not count for that purpose.

The funds distributed don't even have to be returned to the same tax-qualified account. For example, a required minimum distribution from an IRA may be returned to the same account, to a different IRA account, or even to a retirement plan account if the plan sponsor allows it. However, any taxes that were withheld from the original RMD can't be reversed, although they will of course count as payments made when filing your 2020 tax return.

Should I Rollover My 2020 RMD?

Just because you are permitted to rollover the RMD you took earlier this year, doesn't mean you should, even if you can afford to do without this **unneeded required minimum distribution** as a source of cash flow to meet retirement expenses. Depending on your income situation this year and on your income projections for future years, and depending on your outlook for tax rates going forward, this may instead be a relatively opportune year in which to take taxable distributions from retirement accounts.

Work With a Professional

The Case for Roth Conversions in Light of the SECURE Act and Current Market Conditions

The SECURE Act

2019's SECURE Act contains two provisions that make **converting IRAs and retirement plan accounts to Roths** more attractive:

The first of these is that SECURE increases the age at which required minimum distributions must start from 70 1/2 to 72. All else being equal, Roth conversions are more attractive the lower the account owner's current tax rate is relative to that of her (or her beneficiary's) future tax rate. Since most retirees are in relatively low-income years after retirement but before RMDs kick in, this provision of the Act allows these owners of tax-qualified accounts an extra year or two in this "sweet spot" to perform Roth conversions. And now with more of these low-income years over which to spread partial Roth conversions, there is more of a chance to avoid some of the potential negative by-products of this strategy.

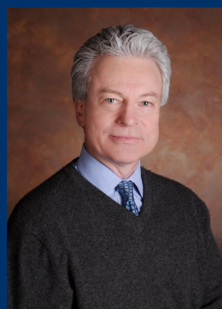
Second, the SECURE Act gets rid of the "stretch IRA" for many beneficiaries. Unless inheritors of tax-qualified accounts are deemed to be "eligible" as defined in the Act (and as discussed in the **last issue of "Seasonal Musings"**), they now have to empty these accounts within 10 years. To avoid being pushed into even higher tax brackets and to avoid some of the other adverse knock-on effects of having higher incomes, many ineligible beneficiaries will want to spread these distributions fairly evenly over this 10-year period. In effect, then, there will be very little remaining tax deferral on a portion of these inherited account balances once the original owners pass away. By contrast, if the original owners had instead converted these tax-qualified account balances to Roths while still alive, their ineligible beneficiaries could opt to wait until the end of the 10th year to distribute the entire inherited account balances tax-free, gaining years of tax deferral in the process.

Current Market Conditions

All else being equal, Roth conversions are also more attractive the higher the expected future returns of the retirement account balance being converted. As alluded to above, Roth conversions are not an "all or nothing" proposition. Owners of more than one tax-qualified account may not only choose which of them to convert, but at least in the case of IRA's, how much of each individual holding within each account to convert. Since **returns on asset classes and on mutual funds tend to revert to the mean**, holdings within an IRA that have not performed very well during the last few years may be prime candidates for conversion. Not only should their future expected returns be relatively high on balance, but the dollar values of these holdings (which determine the tax bill due from the conversion process) should be relatively low.

If we apply these guidelines to what's been going on in the financial markets this year, it may seem like we've missed the boat with respect to Roth conversions. Certainly in retrospect, account balances were more depressed in March and April, which would have been an attractive time to convert, and many investment holdings have now fully rebounded to year-end values and even to all-time highs. However, many asset classes and mutual fund investment styles are still languishing this year and have done so for a number of years. In this respect, investments in small-cap value funds, in international and emerging markets value funds, and in commodities, may still offer attractive opportunities for conversions into Roth accounts.

Take Control of Your Finances



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