WealthInsights

The ABCs of the IRA

Going Beyond a Simple Savings Tool

ROEHL & YI
INVESTMENT ADVISORS, LLC

For A Personal Wealth of Reasons

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Many are familiar with the term individual retirement account, or (IRA) in the United States.

What may not be so obvious, however, is the flexibility this type of account provides for a variety of planning and savings opportunities. In this piece, we will focus on traditional and Roth IRAs.

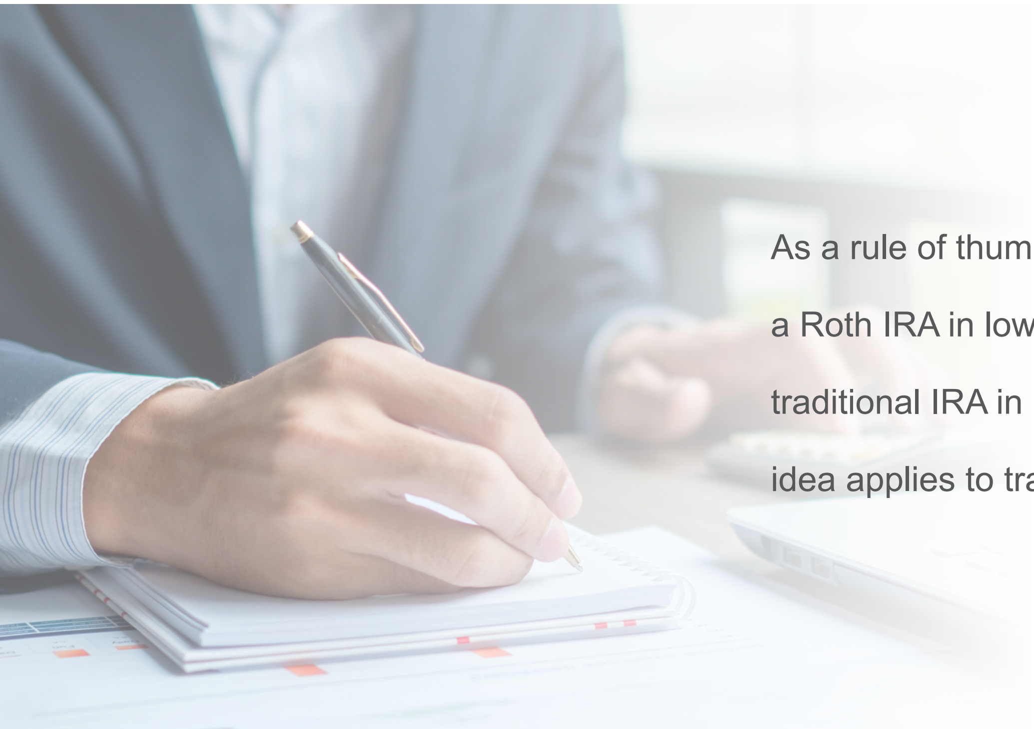
The Basics

The term IRA covers an assortment of account types (some of which may overlap).

Generally speaking, there are ***traditional IRAs*** (funded with pre-tax monies and are subject to the required minimum distribution requirements) and ***Roth IRAs*** (funded with after-tax monies and are not subject to required minimum distribution requirements).

In short, traditional IRAs help lower your taxes today, and Roth IRAs allow you to pay taxes now and have the funds grow tax-free going forward.

NOTE: There are other types of IRAs, such as inherited IRAs (spousal, spousal beneficiary, and beneficiary), SEP IRAs, and SIMPLE IRAs.



As a rule of thumb, it often makes sense to fund a Roth IRA in lower-earning years versus a traditional IRA in higher-earning years. The same idea applies to traditional and Roth 401(k) plans.

How Recent Legislation Has Reshaped IRAs

The rules governing IRAs have undergone changes with The Setting Every Community Up for Retirement Enhancement (SECURE) Act of 2019 and the Securing a Strong Retirement Act of 2022 (SECURE ACT 2.0).

The original SECURE Act moved the age at which required minimum distributions (RMDs) are required to begin from age 70 to 72. An RMD is the amount you are legally required to take out of your account and pay taxes on. SECURE 2.0 moved this back further to age 73 for those born January 1, 1951, or later and to age 75 beginning in 2033.[1]

New Age Requirements for RMDs

Age 70 ½	For births on June 30, 1949, or earlier	Anyone born on June 30, 1949, or earlier should have already started lifetime IRA RMDs and is bound by the original age 70 ½ RMD rule. Nothing changes with the original SECURE Act or SECURE 2.0. Continue to take your annual RMDs as normal.
Age 72	For births on July 1, 1949, through and including December 31, 1950	Anyone born on July 1, 1949, through and including December 31, 1950, should have already started lifetime IRA RMDs and is bound by the original SECURE Act RMD age change to 72. Nothing changes with SECURE 2.0. Continue with your existing RMD schedule.
Age 73	For births on January 1, 1951, through and including December 31, 1959	Anyone born on January 1, 1951, through and including December 31, 1959, will use age 73 as their IRA RMD age. Note that we need a year to adjust to the new age, and 2023 is that adjustment year. People born in 1951 will all turn 72 this year. No RMD is required for these folks in 2023 because the rule is now age 73, and they won't hit 73 until next year. Accordingly, no one will have their very first IRA RMD in 2023, because this year we are transitioning to the new age.
Age 75	For births on January 1, 1960, or later	Doesn't begin for another 10 years (2033).

Source: Slott Report; IRA RMD Age Made Easy.

It is important to note that you may still take distributions from your IRA penalty-free at age 70 ½. Roth IRAs continue not to be subject to an RMD requirement.

A Plethora of Planning Opportunities

IRAs provide a wealth of strategic planning opportunities.

One of the most common goals we hear from clients is a desire to lower taxable income. If someone is participating in an employer-sponsored plan, they may disregard the IRA as a planning tool.

However, anyone may contribute $6,500 to an IRA in 2023 (there is an additional $1,000 catch-up for those age 50 or older)[2] if you have earned income. If you are covered by an employer plan you are subject to the following phaseouts:

Traditional IRA Deductibility (If Covered By Work Plan)	
Single MAGI Phaseout	**$73,000 - $83,000**
MFJ MAGI Phaseout	**$116,000 - $136,000**
MFJ (If only spouse is covered)	**$218,000 - $228,000**

Modified Adjusted Gross Income (MAGI).
Married Filing Jointly (MFJ).
Source: fpPathfinder.com

If you are earning in excess of these amounts you may still contribute, but it will not be tax deductible (also known as a non-deductible contribution).

The Often Overlooked Spousal IRA

Another area of opportunity is the spousal IRA.

If a household has income under $218,000, a spouse can contribute to a traditional IRA even if he or she has no earned income, sheltering $6,500 (or more if you are over age 50) from taxes, provided you file jointly.

If your employer does not have a plan or if you have changed employers and are not yet eligible for the plan, funding a traditional IRA can be a useful tool.

A Deeper Look at Roth IRAs

You can also potentially fund a Roth IRA.

You may fund a Roth, traditional, or a combination of both IRAs up to the annual limit each year. For example, if your income allowed, you could fund $2,000 toward a traditional IRA and $4,500 to a Roth IRA for yourself, but you could not fund $6,500 to a traditional and $6,500 to a Roth.

Roth IRAs are subject to the following annual income limits:

Roth IRA Eligibility	
Single MAGI Phaseout	**$138,000 - $153,000**
MFJ MAGI Phaseout	**$218,000 - $228,000**

Modified Adjusted Gross Income (MAGI).
Married Filing Jointly (MFJ).
Source: fpPathfinder.com

A common frustration for many high-earning individuals is the inability to fund a Roth IRA due to the income limit. The traditional IRA (non-deductible) provides a solution.

Since there is no income limit on non-deductible contributions, an individual above the income threshold can make a non-deductible contribution (after-tax) and then immediately convert to Roth. This essentially achieves the same result as funding a Roth IRA with a few extra steps.

NOTE: What is considered a “backdoor Roth IRA” only works if there is not an existing IRA with tax-deferred assets. The IRS views all traditional IRA assets as one single IRA for tax purposes and applies a pro-rata rule to non-deductible and tax-deferred contributions in these conversions.

Understanding IRA Rollovers

IRA rollovers also provide unique planning opportunities.

You are allowed to make a one-lifetime rollover from an IRA to a Health Savings Account (HSA). The amount is limited to the maximum HSA contribution in the year the rollover occurs, but it can be advantageous as HSA funds are tax-free if they are used for *qualified* medical expenses.

Rollovers can also apply to 529 plans, a tax-advantaged savings plan designed to encourage saving for future education costs. Any unused 529 funds can be rolled into a Roth IRA for the beneficiary.

There are certain restrictions, such as:

- The 529 plan must have been open for 15 years.
- The amount that can be rolled over each year is limited to the annual Roth IRA contribution limits.
- The 529 balance cannot exceed a lifetime limit of $35,000.

Gifting and Charitable Donations

IRAs also provide gifting opportunities.

With the Qualified Charitable Distribution (QCD), distributions made from IRAs of those 70 ½ and older, that are also made directly to qualifying charities, are income tax-free.

Once you reach the age at which you must begin taking RMDs, these gifts to charities can be counted toward your RMDs, thus helping reduce your tax bill. There is an annual limit of $100,000 for the QCD.[3]

Request A Consultation

It is worth remembering that IRAs are multi-faceted tools that may play an important role in your financial planning, beyond what is discussed here.

If you are interested in learning more about IRAs or other financial instruments, please contact Roehl & Yi Investment Advisors and we would be happy to discuss your financial goals.

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[1]Source: Kiplinger, https://www.kiplinger.com/retirement/bipartisan-retirement-savings-package-in-massive-budget-bill

[2]2023 IRA Catch-Up Contribution Limit.

[3]Source: IRS, https://www.irs.gov/newsroom/reminder-to-ira-owners-age-70-and-a-half-or-over-qualified-charitable-distributions-are-great-options-for-making-tax-free-gifts-to-charity