RETIREMENT

Breaking Down the Confusing New Rules About Required Withdrawals from Retirement Accounts

By Elizabeth O'Brien Follow

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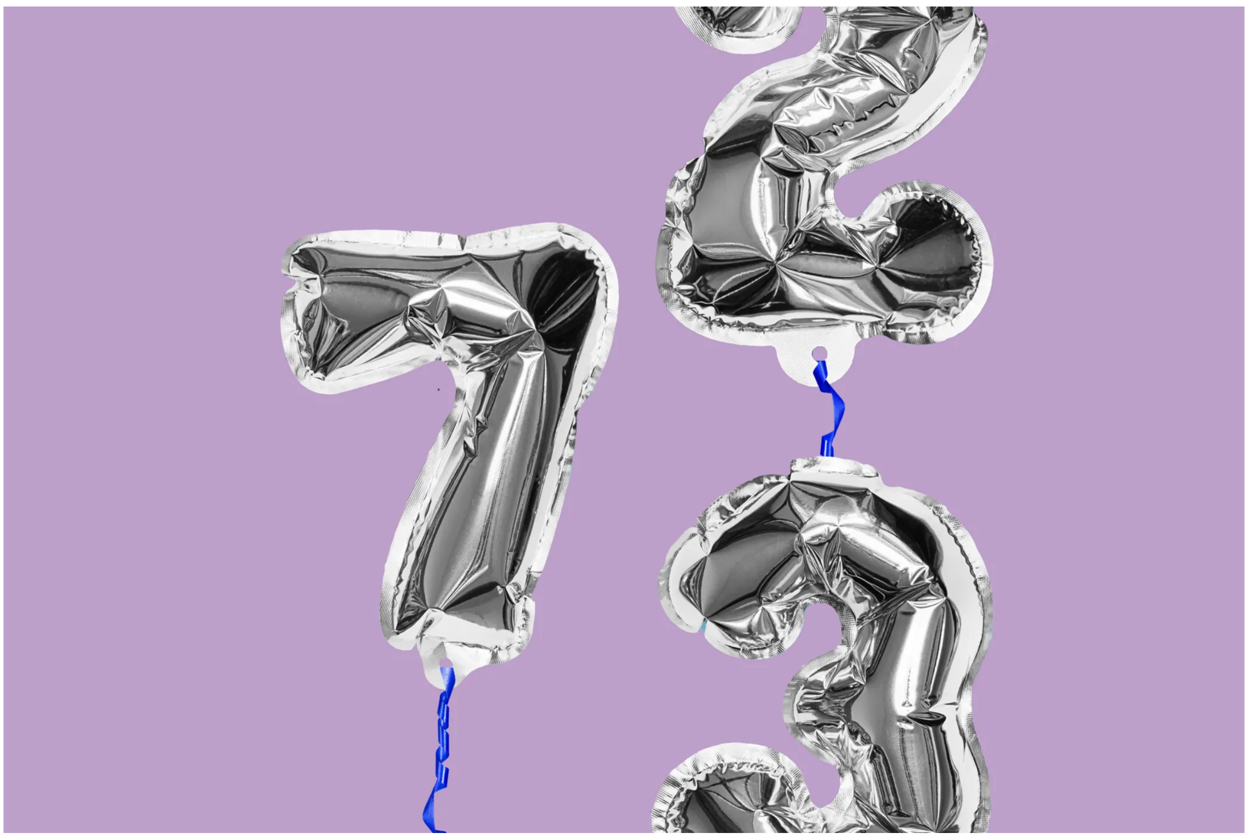

The changing rules around what age retirees need to start tapping their retirement accounts has left some savers confused. BARRON'S ILLUSTRATION; DREAMSTIME

A confusing tax requirement has grown even more so this year, as a new age for required minimum distributions, or RMDs, from retirement accounts takes effect.

Many older adults don't know they must begin withdrawing money from their retirement accounts in their early 70s and paying income taxes on that money. It's the government's way of finally getting a piece of retirement savings that have grown tax-deferred for decades. But even those who are aware of the requirement may not be sure when it begins, since the age has been a moving target: After sitting at age 70 ½ for decades, the Secure 1.0 law of 2019 bumped it to 72. Then came Secure 2.0 in 2022, which raised the age from 72 to 73, effective this year. Starting in 2033, it will rise to 75.

"We always get questions about this, and especially now because the age has increased two times now in four years," says Juan C. Ros, a financial advisor at Forum Financial Management in Thousand Oaks, Calif.

Secure 2.0 gave people who turn 72 this year a brief reprieve; they don't need to take their first RMD until April 1, 2025. (While everyone else must take their annual RMDs by year-end, first-timers have long been given until April 1 of the following year to take their withdrawal for the year they hit the threshold age.)

Put another way, the most recent change affects those born in 1951 or later. Boomers born between 1951 and 1959 must start their RMDs at age 73, while everyone born in 1960 or later will have an RMD age of 75.

Brokerage houses track legislative changes and generally do a good job of telling affected clients how much to withdraw each year to satisfy their RMD requirement, financial advisors say. But there's a caveat, says Stacy Miller, a certified financial planner in Tampa: brokerages only know about the money you have with them. Your RMD is based on your total balance across all retirement accounts subject to the requirement, so if you've got money across several firms, you're going to have to do that calculation yourself or with the help of an advisor.

"The custodian doesn't know about the other accounts, and the advisor might not know either," Miller says.

The penalty for not withdrawing RMDs is 25% of the amount not taken (down from 50% pre-Secure 2.0), with the possibility of a reduction to 10% if the account owner promptly resolves the issue by withdrawing the required amount.

Those who don't need their withdrawal to live on have the option of making a tax-free charitable donation of up to $100,000 to satisfy the RMD requirement (or up to $200,000 for a married couple filing jointly). A qualified charitable distribution (QCD) is transferred directly from an individual retirement account to a qualifying charity, and the amount is not counted toward the donor's taxable income. This could be a boon for higher earners if it prevents them from bumping up a tax bracket or paying income-adjusted Medicare premiums.

The age for QCDs was not adjusted upward with the RMD age and remains 70 ½. This decoupling deepens the confusion around RMDs, but it also yields planning opportunities, says Laura Jansen, a senior wealth advisor with Ironwood Investment Counsel in Scottsdale, AZ.

She has clients who have recently started their QCDs at 70 ½ to get a head start spending down their IRAs and reducing their future RMDs while making a charitable gift.

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