NO MANDATORY IRA WITHDRAWALS IN 2009

This year, you don't have to pull money out and pay the taxes.

You don't have to take RMDs from your traditional IRA this year. On December 23, 2008, President Bush signed the Worker, Retiree, and Employer Recovery Act of 2008 into law, suspending all Required Minimum Distributions (RMDs) from IRAs, 401(k)s and 403(b)s for 2009.[1]

This is sweet relief for people 70½ or older, especially people that don't really need the IRA income. After all, no retiree wanted the "injury" of having to withdraw IRA assets already hurt by the recession plus the "insult" of having to pay taxes on the RMD. You can leave that money in your IRA in 2009 without incurring a tax penalty – and if the markets recover in 2009, those invested assets can grow and compound.[2]

So what if you turned 70½ in 2008? You still have to take your 2008 RMD by April 1, 2009. It should be calculated using your account balance as of Dec. 31, 2007.[2] (This is assuming you haven't taken it already.)

Now, what if you turn 70½ in 2009? Well, you can wait until the end of 2010 to take your first RMD, but the IRS will consider it to be your second RMD.[2]

The IRS says that if you turn 70½ in 2009, you have the option of delaying your first RMD until April of 2010. If you decide to do that, you will have to take two RMDs in 2010: one by April 1, 2010 for the 2009 tax year and one by December 31, 2010 for the 2010 tax year.[2]

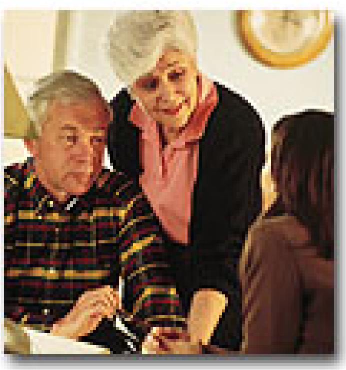
But … since nobody has to take an RMD for 2009, those turning 70½ won't be required to take a 2009 RMD by April 1, 2010. However, you will still have to take a 2010 RMD by December 31, 2010, which the IRS will count as your "second" RMD, even though you didn't take a "first" one for 2009.[2]

How does this affect me if I have an inherited IRA? You may get a break. If the original IRA owner passed away before his or her Required Beginning Date (RBD) – which is generally April 1 of the year after turning 70½ – you face the pesky five-year rule, which requires distribution of all assets in the inherited IRA no later than December 31st of the fifth year after the original IRA owner's death.[2,3] If you are in that situation, you can forego a mandatory withdrawal in 2009 and effectively give yourself an extra year toward that five-year deadline. (If the original IRA owner died after his or her RBD, the timetable of withdrawals is longer; if the initial IRA owner designated a beneficiary, the IRA custodian may permit stretch IRA planning, whereby the beneficiary could receive payments based on their own life expectancy.[4])

What does this mean for IRA charitable rollovers? Suddenly, they've become less attractive for 2009 because of the RMD suspension. (After all, the amount of the charitable rollover counted toward your RMD.) But you can still directly donate to a charity from your IRA this year without incurring income taxes.[2]

And what about Roth conversions? We might as well mention this piece of good news: in 2009, any withdrawals from a traditional IRA can be used to fund a Roth IRA. To convert a traditional IRA into a Roth IRA, your MAGI for 2009 (not including the converted IRA income) has to be $100,000 or lower.[2]

Any chance of no RMDs in 2010? Well, who knows – with 2010 being such an experimental year for the federal tax code, Congress may decide to give older Americans another annual exemption from RMDs. But the odds of that happening seem pretty long. Most likely, traditional IRA owners who are 70½ or older and those who have inherited IRAs or 401(k)s will have to take mandatory withdrawals in 2010.



What does this mean for you? Do you need to take a withdrawal from your IRA, 401(k) or 403(b) in 2009? Should you leave the assets untouched this year? Should they be invested in a slightly different way? What could you do in 2009 to position yourself for 2010, when a horde of taxes will be waived and big tax breaks are available? It's a good time to chat with your financial advisor or tax professional.

Citations

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