Legacy Wealth Management
Group of Las Vegas

Think You Know Your Retirement Assets?
Think Again

For many of us, retirement assets — IRAs and qualified employer plans such as 401(k)s and 403(b)s — will make up the largest portion of our overall investments. We accumulate money into these tax-preferred accounts, and at some point in the future, we will begin drawing from these accounts and paying taxes.

But is that all there is to these assets? Not exactly.

Retirement assets and lifetime tax planning are intertwined. The rules are complex, and the planning opportunities are many. This article will delve into those planning opportunities and how you can take advantage of them while also providing a fresh outlook on paying taxes.

A Different Way of Looking at Taxes

Tax planning involves taking tax-efficient steps to strengthen a long-term financial plan. The main thrust of traditional tax planning has been to reduce taxes to the greatest extent possible today and worry about it later — in essence, kicking the "tax can" down the road. That is why there is an emphasis on making pre-tax retirement contributions today to lower tax liability in the current year, which is solid advice.

While it is important to keep taxes low on a year-by-year basis, doing so can lead to some of the challenges addressed earlier, such as accumulating substantial pre-tax assets that will need to be taxed at some point.

That is why our preferred approach is *lifetime tax minimization*, not necessarily year by year. This is taking a bird's eye view of a client's taxes.

By smoothing the tax liability over a client's lifetime — rather than reducing taxes now and then having to pay more later — we can better control a client's sources of income from the portfolio while also avoiding a potential "tax bomb" in retirement.[1]

Tax Planning Principles:

- **Required minimum distributions are just the minimum**

When the IRS mandates that a certain amount must be taken from an IRA, that mandate is just the minimum — hence the term "required *minimum* distribution." But there are reasons to consider taking out *more* than the required amount. It would mean paying more in tax but would also be reducing the size of a pre-tax IRA. Also, there may be room in the current tax bracket to absorb that extra income before bumping into a higher tax bracket.

Note that whether to take more than the required amount — and how much more — is an analysis that ideally should take place each year in the fall with the help of a tax preparer and your advisor.

- **Accepting higher taxes today for future benefits.**

This goes back to the earlier point about smoothing out tax liability over a lifetime, such as taking more than the required amount from an IRA or doing a strategic Roth conversion (see the next section). Both of these are voluntary actions that will increase current-year tax liabilities. While no one likes paying taxes, if it means a better outcome over the long run to pay a little more today, then it should be considered.

Understanding Strategic Roth Conversions

A Roth conversion is the transfer of assets from a pre-tax IRA into a Roth IRA. Income tax is due on the amount that is converted into the Roth IRA. Once inside the Roth IRA, the money grows tax-free and is distributed tax-free. If inherited, beneficiaries do not pay tax either.

Why would someone do a Roth conversion? There are several reasons:

- *Prepay the income tax for children*
- *Reduce the balance of a pre-tax IRA prior to being required to take distributions from it*
- *Pay taxes now while in a lower tax bracket when likely to be in a higher tax bracket in the future*
- *Tax diversification — different types of accounts are treated differently for tax purposes — to have flexibility in retirement for drawing income*

Roth IRAs can be powerful tools for cash flow, tax and estate planning. What makes a Roth conversion strategic is the use of low tax brackets in low-income years to maximize the value of the conversion.

In other words, there are benefits associated with paying a little more tax now — thanks to a Roth conversion — rather than paying less now and much more later without doing Roth conversions. *The goal with strategic Roth conversions is to smooth taxes over a retiree's lifetime*, as opposed to allowing required minimum distributions to push retirees into higher tax brackets as they age.

This is easier said than done. **Fortunately, your advisor can help determine what an ideal Roth conversion amount would be year to year.**

Inherited IRAs: The Good, the Bad, the Ugly

One area of retirement accounts that has received a lot of attention lately is that of inherited IRAs — accounts created for the benefit of beneficiaries after the death of the original account owner. Between recent legislation passed by Congress and new regulations published by the IRS, the rules for inherited IRAs have become quite confusing. That is the ugly of inherited IRAs — the rules are rather complicated, having changed significantly since 2019, and it can be difficult to understand all the nuances without guidance.

For most non-spouse beneficiaries, with few exceptions, inherited IRAs will have required minimum distributions annually and must be completely distributed by the end of the 10th year following the death of the original account owner. For those with sizable pre-tax inherited IRAs, that could mean large taxable distributions. That is the bad — pre-tax inherited IRAs are not great for tax-paying beneficiaries. (However, pre-tax IRAs are excellent assets to leave to charity.)

The good is that inherited *Roth* IRAs are great for beneficiaries. While most non-spouse beneficiaries will still have to deplete the inherited Roth by the 10th year following the death of the account owner, none of the required distributions during those 10 years is taxable. To the extent funds remain in the inherited Roth, that money can continue growing on a tax-free basis until required to be distributed.

That is why doing strategic Roth conversions can be so beneficial to the next generation — inheriting Roth IRA assets may provide advantages compared to pre-tax IRA assets.

Sources

1 For an in-depth look at the retirement "tax bomb," see the series of articles authored by Forum Partner David McClellan **here**.

Greg Feese, CRPC®

Legacy Wealth Management Group
Las Vegas
greg@legacywmglv.com
(702) 545-0680
www.legacywmglv.com

Joseph M Kloeckner

Legacy Wealth Management Group
Las Vegas
jkloeckner@legacywmglv.com
(702) 545-0680
www.legacywmglv.com

Our normal hours of operation are
Monday - Thursday 8:00am - 4:30pm & Friday 8:00am - 3:00pm

Advisory Services offered through PR Wealth Management Group, Inc., a Registered Investment Advisor. PR Wealth Management Group, Inc., a Registered Investment Adviser, doing business as Legacy Wealth Management Group of Las Vegas, LLC. PR Wealth Management Group, Inc. only transacts business in states where it is properly registered or notice filed, or excluded or exempted from registration requirements. This is not a solicitation for sale of securities in any jurisdiction.. The investment advisory representatives referred to on this site may only transact business, effect transactions in securities, or render personalized investment advice for compensation, in compliance with state registration requirements, or an applicable exemption or exclusion.

Legacy Wealth Management Group of Las Vegas | 8235 S. Eastern Ave. , Suite 160, Las Vegas, NV 89123 | 702-545-0680
Visit our website