Cherry Tree Wealth Management

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CHERRY TREE WEALTH INSIGHTS: *Published by Keith Tufte, President of Cherry Tree Wealth Management, LLC, with insights on investing and wealth management.*

INVESTING QUOTE OF THE MONTH:

"Two essentials for successful retirement are sufficient funds to live on and sufficient things to live for." – Ernie Zelinski

CARES ACT WAIVES 2020 REQUIRED IRA DISTRIBUTIONS

The U.S. recently passed the 2020 Coronavirus Aid, Relief, And Economic Security (CARES) Act, a huge $2 trillion emergency fiscal stimulus package in response to the COVID-19 pandemic and recession. This act contains a wide variety of loans, rebates, tax credits, cash payments, unemployment benefits, and small business benefits to help families and companies. This note will focus on the rule change for 2020 that waives required minimum distributions (RMDs) from retirement accounts such as IRAs and 401K plans. It applies to all types of IRA accounts including inherited IRAs. This change waiving the RMD requirements for 2020 will affect many of our clients and/or their parents.

WHY SKIP YOUR 2020 RMD?

The main reason to skip taking your RMD in 2020 is to defer income taxes. Let's say your 2020 RMD is $20,000 and your total (Federal + State) marginal income tax rate is 30%. That $20,000 IRA distribution is taxable at your full ordinary income tax rate creating a tax liability for you of $6,000. By skipping the RMD this year you would save $6,000 in income taxes, a pretty nice deal. By not taking the taxable IRA withdrawal you are letting the IRA assets continue to grow tax-deferred for another year.

WHO SHOULD SKIP TAKING THEIR 2020 RMD?

People who we think are best positioned to skip taking their RMDs in 2020 are as follows:

1. **Wealthy people who don't need the RMD cash withdrawal for living expenses.** These people have plenty of other income and assets and are not using the RMD each year for living expenses. In previous years they have typically been taking their RMD, withholding the income taxes on the distribution, and then reinvesting the balance into another investment account.

2. **Inherited IRA owners.** Inherited IRA accounts are typically smaller, and the RMD amounts are also typically much smaller in dollar terms. These people are often younger, still working, and are not using their Inherited IRA distributions each year for living expenses.

3. **People who are in high marginal income tax brackets with significant other income and assets.** Some people are in relatively high tax brackets due to large pension income, social security income, earned income (if still working) and other investment income when retired. They also may live in a high tax state like Minnesota, New York or California. These people might consider avoiding taking the 2020 RMD as they probably don't need the income and the RMD will get taxed at a fairly high rate. They can take money from other accounts if they need it for living expenses.

4. **People whose IRA assets are a relatively small part (perhaps 25% or less) of their total retirement portfolio.** These people can skip taking the RMD in 2020, avoid the income tax on it, and withdraw from their other accounts if they need living expenses.

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WHO SHOULD KEEP DOING THE REGULAR RMD THIS YEAR?

Many people will continue taking their RMD in 2020 just like they have been every year, even though they don't HAVE to take it this year. Usually this will be because people want/need the income from the RMD for normal retirement living expenses. People whose IRA assets are a significant part (50%+) of their total retirement portfolio will probably need the cash from the RMD for normal living expenses. If you are in a relatively low retirement income tax bracket, taking the RMD this year is not such a bad choice. If you think your future income and tax rate will go up, it can be smart to take your RMD this year (at the relatively lower tax rate). Taking your RMD this year will reduce your future year RMDs slightly, and the taxes associated with those future RMDs.

YOUR 2020 IRA RMD IS UP TO YOU—IT IS NOT ALL OR NOTHING

Keep in mind the change only means you are not required to take a certain amount from your IRA. That allows you to take any amount (including none) from the account. What could be smart for some is to take a partial (taxable) withdrawal this year. People may want to do this because they need or want to have some of the cash from the IRA for living expenses, but they don't need the full amount and they want to save some income taxes. Start with our previous example where your full RMD for 2020 is $20,000. You could choose to take half of it as an IRA distribution this year ($10,000) for living expenses, and you would still save $3,000 in income taxes by not taking the full $20,000 IRA RMD.

QUALIFIED CHARITABLE DISTRIBUTIONS (QCD) FROM YOUR IRA?

Several of our clients have been using part of their IRA RMD each year as charitable donations. This is a very smart way to give to charities because the part of the RMD that you donate to charity is excluded from income tax this year. We think doing these qualified charitable distributions is still one of the most tax-efficient ways to give to charity for many people (along with giving away appreciated securities). We recommend many people continue to gift this way. For those people who don't need the IRA distribution for living expenses, they could continue to give the part of the RMD to charity as they were before, and then skip the rest of the RMD this year. Using our example of the $20,000 full RMD for 2020, you could gift $10,000 of that to charity using the QCD strategy (saving $3,000 in income tax), and then skip taking the rest of the $10,000 RMD for the year (saving another $3,000 in income tax).

Did this couple skip their 2020 RMD and spend the tax savings on a scooter?

We hope this is a helpful guide in terms of things to consider when deciding how much (if any) of your 2020 required minimum distributions you should take. We would be happy to discuss the best strategy for you regarding your IRA RMDs, or how any of the other provisions of the 2020 CARES Act might apply to you or your family. Call or email us anytime to discuss or to set up a meeting.

Cherry Tree Wealth Management, LLC (CTW) provides unique wealth management services for a select group of client families to help give them peace of mind. Author Keith Tufte, (President of CTW) has over 25 years of successful investment management experience as a Wall Street Analyst, Mutual Fund Portfolio Manager, Director of Equity Research for a major mutual fund firm, Hedge Fund Portfolio Manager, and Wealth Management Advisor. Please FORWARD this e-mail to friends/relatives/business associates that you think may have an interest. Please see our website at http://www.cherrytree.com.

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WEALTH MANAGEMENT

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