Elder Law Guys: If you own an IRA, this is for you

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Avid readers of this column (yes, there are some) may recall that in our January 2020 column we discussed the then-upcoming implementation of the Secure (Setting Every Community Up for Retirement Enhancement) Act which affected anyone who owns an IRA and would die after Jan. 1, 2020.

Wait a minute, that affects almost all of us — and it's trillions of dollars — that are going to be taxed after decades of kicking the can down the proverbial income tax road.

Common versions are 401Ks, 403s, 457s and the traditional IRA (or Individual Retirement Account). All of these plans eventually morph into an IRA. So, for simplicity's sake, we will refer to all of these plans as "IRAs."

So, what happened over the last couple of years that moves people to deal with income tax realization on collectively trillions of dollars?

Simple: The IRS has spoken, or at least muttered its anticipated proclamation on the implementation of the infamous Secure Act. Admittedly, the language in the original law did not specifically say how it works in practice and it left many of us scratching our heads.

Practically speaking, for those IRA owners who died leaving beneficiaries since that date, the question was, "How is the Required Minimum Distribution (RMD) determined from that IRA?"

The RMD is the amount an IRA owner must pay tax on each year to avoid the dreaded 50% "excise tax" that should have been withdrawn. This rule applies to the original IRA owner who reaches age 72, as well as those who survive the original owner and inherit said IRA.

Sound complicated? Well, it is for most of us.

Fast forward since the implementation of the Secure Act of 2020. On Feb. 24, the IRS issued its proposed regulations on RMDs.

Ah, it's about time.

Statistically, people owning IRAs have obviously still been dying since Jan. 1, 2020. Throw in a once-in-a-century pandemic that accelerated mortality rates and you've got a recipe for a crash course in how this new law is supposed to work. Even though these regulations are "proposed," history shows we can rely upon such proclamations from the IRS as the expected final rules — for the most part.

If the proposed regulations issued by the IRS are close to what the final rules will be, what should millions of U.S. citizens do to handle the trillions of dollars to be taxed of the next few years?

Simple: Plan now.

This IRS publication is more than 270 pages long and far be it from us to explain all the nuances in this column. However, the important takeaway is planning in advance is required for anyone with an IRA.

Because of the decades-old rules on IRAs, we have been guided to handle our own retirement through these deferred taxation plans. To properly account for the options and the proposed rules, an IRA owner must look at both their lifetime needs and tax issues as well as those who will someday inherit in order to minimize various tax exposures.

Not too long ago, many people thought a well-rounded estate plan consisted of preparing a few basic legal documents such as a will and various powers of attorney. However, the paradigm shift of wealth to IRAs over the past few decades forces us to rethink how to integrate one of the most valuable assets of our net worth into a proper estate plan.

Remember, it is worth noting your will typically does not determine who receives your IRA at death.

These new regulations will force us to think about things like Roth conversions and Generation Skipping Trusts and other more complex ways to reduce overall tax exposure to our IRAs. One thing is certain — the government has shown its hand in accelerating the realization of income tax on your life savings.

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