12 IRA Mistakes

Help Clients Avoid Common and Costly IRA Pitfalls

Stephen Gilbert, CFP®, CLU®, ChFC®, RICP®, CASL®, CRPC®
Vice President of Advanced Planning

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Prudential

The IRA Market

The State of the Rollover and Retirement Income Markets

- The Current IRA Market: $11.5 Trillion[1]
- Annual Dollar value of rollovers: $536 Billion[2]
- 85% of households rolled over the entire retirement plan balance to their IRA[2]

1. ICI Quarterly Retirement Market Data, Fourth Quarter 2023, March 16, 2023
2. ICI Research Perspective, "The Role of IRAs in US Households' Saving for Retirement. 2022"; February 2023; Vol. 29, No. 1; Rollover data for 2019 (latest available year)

Common and Costly IRA Mistakes

- Not Contributing
- Excess Contributions
- Rollovers
- Early Distributions
- Distributions in Down Markets
- Excess Withdrawals
- RMD Mistakes
- NUA (Net Unrealized Appreciation) Mistakes
- Beneficiary Reviews
- Trust as Beneficiary
- Beneficiary Mistakes
- Roth IRA Mistakes

Not Contributing Enough

- Failing to make Catch Up Contributions if over 50
- Failing to make Non-Deductible Contributions if income exceeds limit to contribute to a Deductible or Roth IRA
- Failing to contribute to a Spousal IRA
  - Up to $6,500 ($7,500 if age 50 or above) 2023
  - Up to $7,000 ($8,000 if age 50 or above) 2024
  - Married couple must:
    - File joint tax return
    - At least one spouse earns as much as the amount contributed to all IRAs
    - Catch up contribution can only apply to spouse/s age 50 or over
- Under the SECURE Act taxpayers with earned income can contribute to an IRA regardless of age in tax years after December 31, 2019

Excess Contributions

Contribution Limits 2023/2024

- ❑ $6,500–2023, $7,000-2024
- ❑ $1,000 Catch Up for 50 and older
- ❑ Contribution deadline: Tax filing deadline, excluding extensions

How Excess Contributions Happen

- ❑ Exceed annual limit
- ❑ More than earned income
- ❑ Ineligible rollover (RMD, SEPP)
- ❑ Roth IRA contribution made when MAGI exceeded income limits

6% Penalty for each year excess amount remains in the IRA

Rollover Mistakes

- Failing to Complete Rollover in 60 Days
- Ineligible Rollover (RMDs, SEPP, Annuitized Income)
- Incorrect Transfers of Inherited IRA
- More Than One Rollover within 365 Days
- Rolling over After-Tax Contributions to a Traditional IRA

Indirect Rollovers

- 20% mandatory tax withholding on eligible rollover distributions from qualified plans
- Within 60 days
- Only one IRA-to-IRA rollover allowed in 365 days
- Reported on 1099-R & 5498

Direct Transfers

- Institution to institution
- No withholding
- No 60-day requirement
- Not limited to once per 365 days
- Not reportable

Reasons to Roll to an IRA

- No plan-imposed restrictions
- Estate strategy benefits
- No mandatory 20% withholding on withdrawals
- Control and greater investment selection
- Access to products providing protection against market declines and the potential for income in retirement*

* All references to guarantees, including the benefit payment obligations arising under the annuity contract guarantees, rider guarantees, any fixed account crediting rates or annuity payout rates are backed by the claims-paying ability of the issuing insurance company. Those payments and the responsibility to make them are not the obligations of the third-party broker/dealer from which this annuity is purchased or any of its affiliates.

Reasons Not to Roll to an IRA

- Early Access to Retirement Assets

  Retired at or after age 55

- Delayed Distributions

  After IRA Required Beginning Date* and still working

- Net Unrealized Appreciation (NUA) Tax Treatment
- ERISA Creditor Protection

* Taxpayers must begin distributions by their Required Beginning Date which is April 1 of the year following the year the taxpayer reaches their "applicable age"

If the taxpayer was born …	Before July 1, 1949	After June 30, 1949 and before 1951	After 1950 and before 1960*	After 1959*
The "applicable age" is …	70½	72	73*	75*
*Based on a recent clarification, the RMD age for those born in 1959 appears to be age 73."				

Taking an Early Distribution

10% Additional Tax Unless One of the Exceptions Below Apply

- Age 59 ½
- Death or Disability
- First time home buyer (up to $10,000)
- Deductible medical expenses (in excess of 7.5% of AGI)
- Education expenses for investor’s family
- Health insurance premiums for the unemployed
- Substantially equal periodic payments

Early distribution after divorce is not an exception

Not all exceptions are listed
Not all of these exceptions apply to employer-sponsored qualified plans

Taking Distributions in a Down Market

1 **What is a bear market?**
– 20% loss from the most recent market peak*
– 12 bear markets since 1945*

2 **What is the average bear market loss since 1945?**
– 35%**

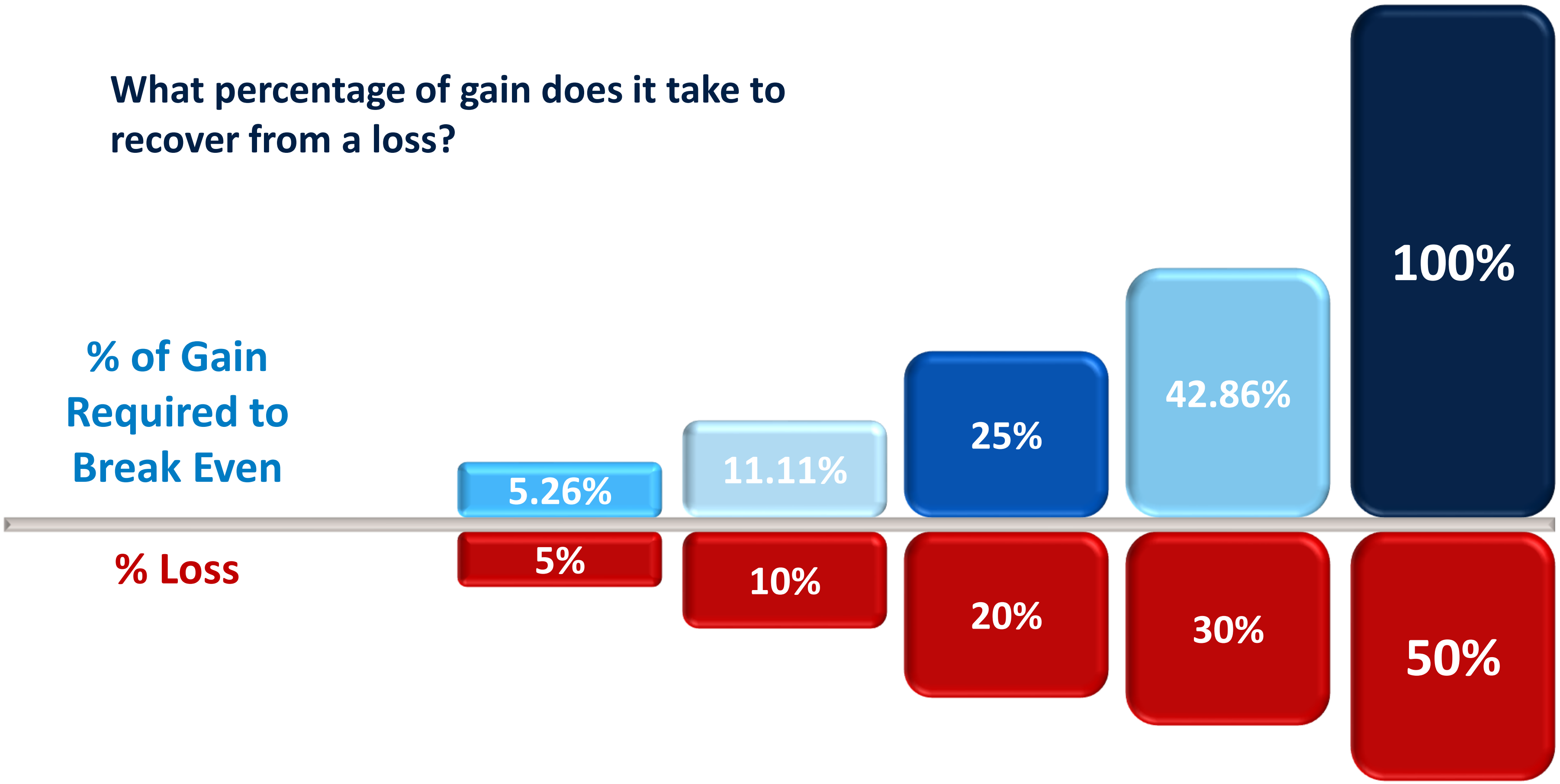
3 **Historically, how many bear markets have retirees faced on average?**
– 4 bear markets***

4 **Historically, how long has the average bear market lasted?**
– 16 months*

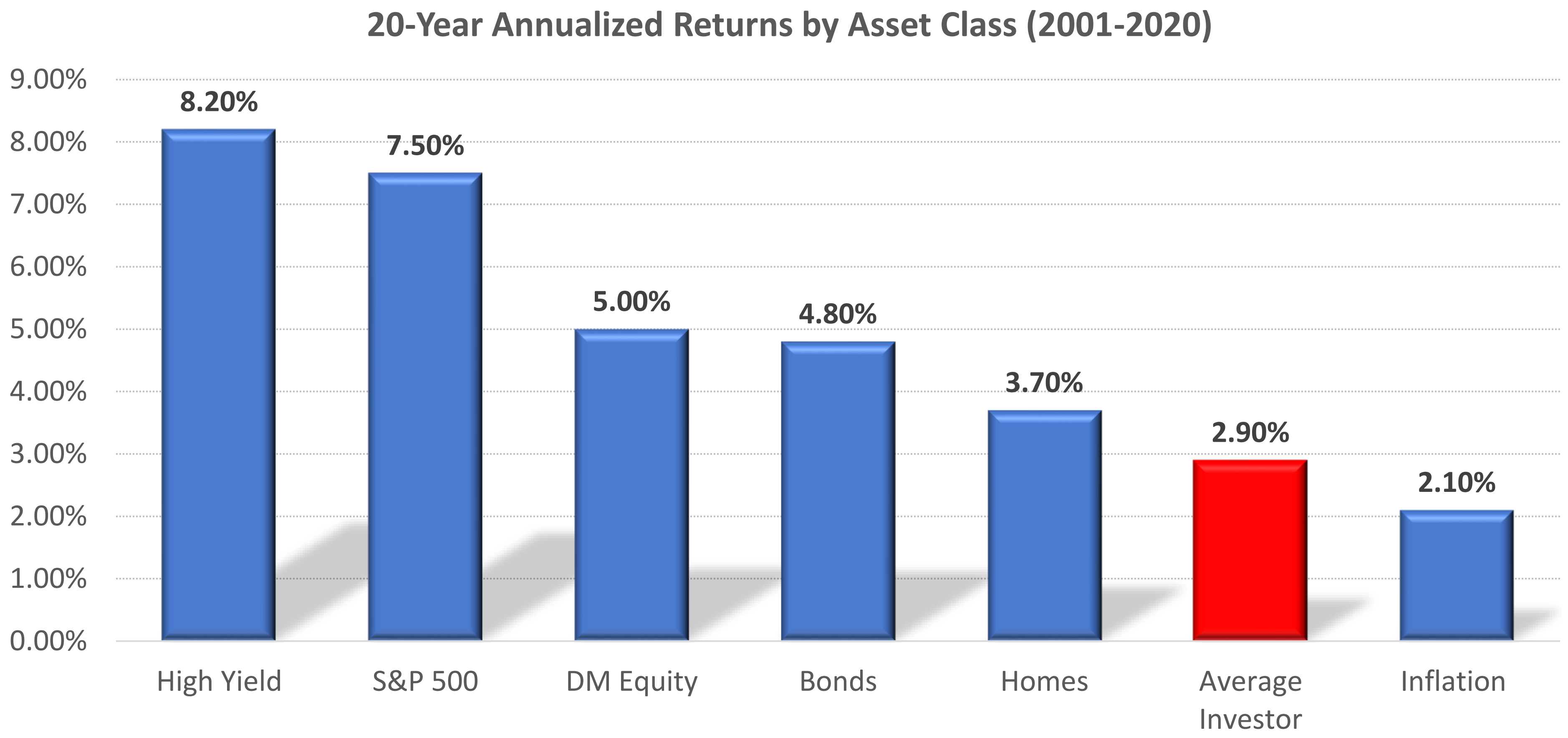
* JP Morgan "Guide to the Markets®", 1Q 2023; based on market activity post-WWII
** Does not include losses from the 2022 bear market cycle
*** Assumes retiree age 65 with anticipated death at age 90, and an average 7.4 years between market peaks in the post-WWII era. Does not include the 2022 bear market cycle.
Historical data does not predict future results.

Market Risk

Mathematics of loss in accumulation



Investor Behavior Risk

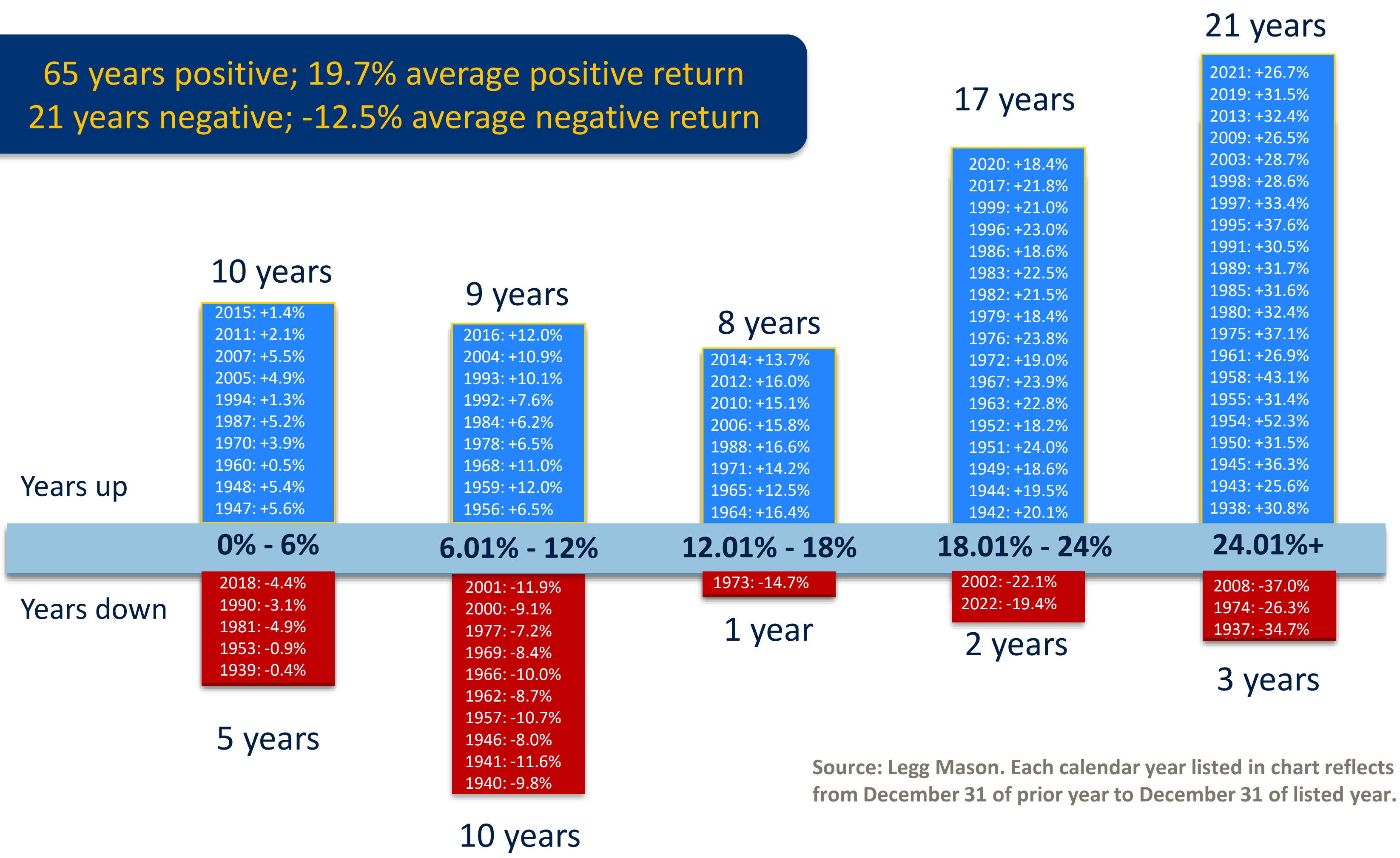


Source: Barclays, Bloomberg, FactSet, Standard & Poor's, J.P. Morgan Asset Management; (Bottom) Dalbar Inc, MSCI, NAREIT, Russell.
Indices used are as follows: DM Equity: MSCI EAFE, Commodity: Bloomberg Commodity Index, High Yield: Bloomberg Barclays Global HY Index, Bonds: Bloomberg Barclays U.S. Aggregate Index, Homes: median sale price of existing single-family homes, Inflation: CPI. Average asset allocation investor return is based on an analysis by Dalbar Inc., which utilizes the net of aggregate mutual fund sales, redemptions and exchanges each month as a measure of investor behavior.. Guide to the Markets – U.S. Data are as of March 31, 2022

Rewards of Long-Term Investing

Positive versus negative average annual returns for the S&P 500 (1937-2022)

65 years positive; 19.7% average positive return
21 years negative; -12.5% average negative return



Source: Legg Mason. Each calendar year listed in chart reflects average annual performance from December 31 of prior year to December 31 of listed year.

Indexed Variable Annuities

Point to Point Cap Rate Strategy			
	Term	**Cap Rate**	**Buffer**
S&P 500	1 year	20%	10%
S&P 500	3 year	Uncapped	10%
S&P 500	6 year	Uncapped	20%

Step Rate Strategy				
	Term	**Step Rate**	**Participation Rate**	**Buffer**
S&P 500	1 year	11.5%	80%	5%

Accelerated Participation Rate Strategy					
	Term	**Tier Level**	**Tier 1 Rate**	**Tier 2 Rate**	**Buffer**
S&P 500	6 year	20%	100%	115%	10%

Hypothetical example of an Indexed Variable Annuity illustrating some of the different cap rate and buffer strategies typically offered by these products.

Withdrawal Rate Risk

What is a Safe and Sustainable Withdrawal Rate?

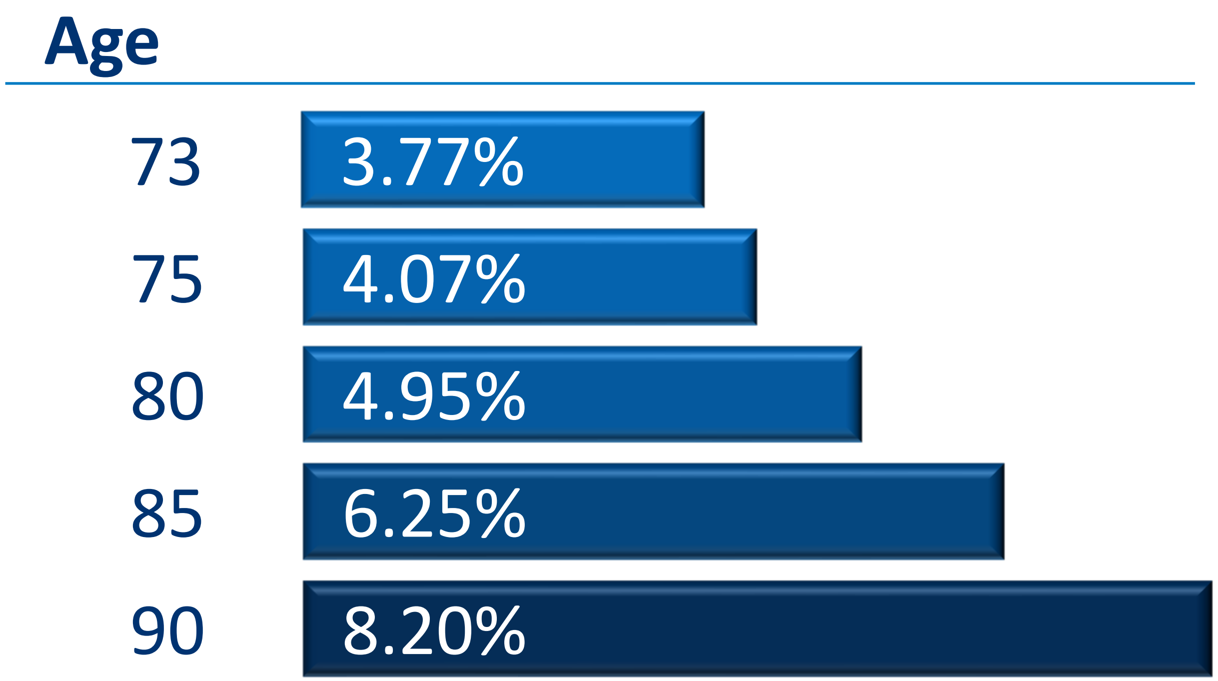
The rate one can safely withdraw from their retirement portfolio without prematurely depleting the account

Bengen (1994)[1]:	**4%**
Guyton (2004)[2]:	**3.6% - 5.8%**
Milevsky & Huang (2010)[3]:	**3%**
Pfau (2021)[4]:	**2.7%**

1. "Determining Withdrawal Rates Using Historical Data", William Bengen, Journal of Financial Planning, October 1994
2. "Decision Rules and Portfolio Management for Retirees: Is the 'Safe' Initial Withdrawal Rate Too Safe?", Jonathan Guyton; FPA Journal; October 2004
3. "Spending Retirement on Planet Vulcan: The Impact of Longevity Risk Aversion on Optimal Withdrawal Rates"; M.A. Milevsky & H. Huang; Retirement Income Journal, March 2010
4. "Retirement Income Dashboard For a Benchmark Couple Both Turning 65 in January 2023"; Conservative portfolio (25% stock allocation) with 2% spending COLA; Wade Pfau at https://retirementresearcher.com/dashboard/

RMDs and Sustainable Withdrawals

RMDs Increase Each Year*



***If the spouse is the sole beneficiary and is more than 10 years younger, the RMD distribution rate is lower.at each age**

RBD is generally April 1 of the year following the year the IRA owner reached the applicable age

The Applicable Age is determined based on the following:

If the taxpayer was born …	Before July 1, 1949	After June 30, 1949 and before 1951	After 1950 and before 1960*	After 1959*
The “applicable age” is …	70½	72	73*	75*
*Based on a recent clarification, the RMD age for those born in 1959 appears to be age 73.”				

Required Minimum Distribution Mistakes

$$\text{RMD} = \frac{\text{Fair Market Value}}{\text{Life Expectancy Factor}}$$

“Fair Market Value” aka “Entire Interest” = Annuity cash value plus Actuarial Present Value of contract benefits

Required Beginning Date

- April 1 of the year following the year the individual attains “applicable age”

  If deferred until the following April, two RMDs will have to be taken that year.

If the taxpayer was born …	Before July 1, 1949	After June 30, 1949 and before 1951	After 1950 and before 1960*	After 1959*
The “applicable age” is …	70½	72	73*	75*
*Based on a recent clarification, the RMD age for those born in 1959 appears to be age 73.”				

Penalty for missing RMD:

- 25% penalty of the amount that should have been withdrawn*
- Correct with IRS Form 5329

* Penalty may be reduced to 10% if the missed distribution is corrected timely

Exception to RMDs

- Roth IRA
- Annuitized IRA
- Qualified Charitable Distributions
  - Not taxed (but reported) to owner
  - Satisfies RMD
- Qualified Longevity Annuity Contracts (QLAC)
  - Can defer income until age 85
  - Up to $200,000
  - Reduce RMD at age 73 by over $7,500

RMD Aggregation Rules

Multiple IRA Accounts

- RMD must be calculated separately for each account but the RMD can come from any one, or any combination, of IRAs

Multiple 401(k) Plans

- Each plan is treated separately for calculating and distributing RMD

Net Unrealized Appreciation Mistakes

Qualified Employer Stock

Cost Basis (Taxed as Ordinary Income)

NUA (Taxed as Capital Gains)

Stock must be taken "in-kind", pursuant to a complete liquidation

Do not:

- **Rollover stock**
- **Take a partial distribution or a partial rollover after occurrence of trigger event**

Failure to Conduct Beneficiary Reviews

Retirement assets account for 38% of the wealth for Americans with a net worth of $100,000 or more*

- Wills only cover probate assets
- Review beneficiary designations after life changing events
- Dangers of naming trusts as beneficiary of retirement accounts

*United States Census Bureau, Net Worth and Asset Ownership of Households 2020; Source 2020 Survey of Income and Program Participation
Weighted average households with net worth over $100,000; includes home equity; 69% when excluding home equity

Dangers with Naming Trust as Beneficiary

- Failure to draft Trust to be a "look through" trust could cause payout under 5-year rule
- Failure to specify income payable to trust beneficiaries (RMD only or all trust income)
- To the extent trust is not mere conduit, any IRA assets remaining in trust will be taxed at the trust rates

37% for income above $14,450-2023, $15,200 - 2024

Plus 3.8% Medicare Surtax† - Totaling 40.8% Tax

- Under the SECURE Act, many trusts will be required to liquidate beneficiary IRAs fully within 10 years

* IRS Rev. Proc. 2022-48; IRB 2022-45, November 7, 2022

† IRA distributions are not subject to the 3.8% surtax on investment income.

Split to Maximize Payout Options

IRAs with Multiple Beneficiaries

- Failure to split the account to take advantage of the “separate accounts rule” could result in beneficiaries being forced to use the life expectancy of another individual to calculate stretch payments, or force a beneficiary entitled to stretching to take distributions under the 10-year rule.
- Split by December 31st of the year after death
- Split if there are **Multiple Beneficiaries**
- Split if a **Non-person Beneficiary**

Roth Conversions

Benefits & Considerations

Benefits

- Increase Tax-free Savings
- Hedge Against Rising Taxes
- Estate Strategy Benefits
- Tax Diversification
- No RMDs

Considerations

- Time Horizon
- Current Tax Bracket
- Tax Rates when Retired
- Paying the Conversion Tax Liability

The Pro-Rata Rule

Multiple IRAs Must be Aggregated for Roth Conversions

- $80,000 Taxable IRA
- $20,000 Non-Deductible IRA (no earnings)
  - In the aggregate there is $100,000 IRA, 80% taxable, 20% tax-free
  - If the $20,000 non-deductible IRA is converted, 80% will be subject to an income tax
    - Could roll $80,000 IRA to a 401(k) plan to avoid aggregation rule

Must file IRS Form 8606 in any year Non-deductible money is added to or withdrawn from the IRA

Roth Conversion of After-tax 401(k) Contributions

IRS Notice 2014-54: plan participants can roll pretax contributions to traditional IRA, after-tax to a Roth IRA

- Not all plans permit after-tax contributions.
- Not subject to **$22,500*** cap ($23K – 2024) for pre-tax/Roth deferrals (**$30,000** if age 50 or over) ($30,500 – 2024)
- Subject to the **$66,000*** ($69K – 2024) overall plan contribution limits (**$73,500** for those age 50 or over) ($76,500 – 2024)
- After-tax contributions subject to non-discrimination test
- Plan must permit in-service withdrawals of after-tax contributions, or the participant is otherwise eligible to take a distribution

* For 2023; indexed for inflation

Using RMDs to Finance Roth Conversions

Client subject to RMD's but does not want/need income.
Seeks to leave tax advantaged account to heirs.

Strategy:
Use after tax RMD amount to finance annual ROTH Conversion within IRA.

Benefit:
Reduce RMD's over time
Provide TAX-FREE ROTH to heirs.

Using RMDs to Finance Roth Conversions

Year	IRA	RMD	After Tax (24% Tax)	Conversion	Conversion Tax (24%)	Roth w/6% Growth
1	$1,000,000	$37,736	$28,679	$119,497	$28,679	$126,667
2	$893,333	$35,033	$26,625	$110,937	$26,625	$251,860
3	$792,206	$32,203	$24,475	$101,978	$24,475	$375,068
4	$697,506	$29,431	$22,367	$93,197	$22,367	$496,361
5	$609,371	$26,610	$20,224	$84,265	$20,224	$615,463
6	$528,405	$24,018	$18,254	$76,058	$18,254	$733,013
7	$454,028	$21,518	$16,354	$68,140	$16,354	$849,222
8	$386,233	$19,120	$14,532	$60,548	$14,532	$964,357
9	$324,958	$16,750	$12,730	$53,043	$12,730	$1,078,443
10	$270,474	$14,620	$11,111	$46,297	$11,111	$1,192,225

Assumes 24%marginal tax bracket; also assumes a net 6% return on IRA and Roth IRA assets; Distributions and conversion occur at beginning of year. Assumes initial RMD age is 73, and takes place after 12-31-2021.

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Conclusion

The IRA Rollover Market

Continues to Grow

Greater Concern About the

Distribution Phase

of Retirement Planning

Financial Professionals That Are

"Knowledgeable of IRAs"

Will Be Most Successful

Be the Financial Professional of Choice

Disclosures

Investors should consider the features of the contract and the underlying portfolios' investment objectives, policies, management, risks, charges and expenses carefully before investing. This and other important information is contained in the prospectus, which can be obtained by contacting the National Sales Desk. Clients should read the prospectus carefully before investing.

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Disclosures

Conversions to a Roth IRA are generally fully taxable. Before clients convert to a Roth IRA, consider how their tax bracket will affect the overall benefit of the rollover. Conversion income may push them into a higher tax bracket. It is, however, possible to convert only part of their traditional IRA. This could enable them to remain in the same tax bracket they would be in without the conversion.

It is generally advisable to pay the taxes on the conversion with funds other than those in a client's traditional IRA. If clients are under age 59½ when they do a conversion, any funds not deposited in the Roth IRA will be subject to the 10% additional income tax (unless an exception applies).

Because qualified retirement plans, IRAs, and annuities offer a tax-deferral feature, clients should carefully consider the other features, benefits, risks, and costs associated with an annuity before purchasing one in either a qualified plan or an IRA. Before purchasing an annuity, clients should take full advantage of their 401(k) and other qualified plans.

S&P 500® Index is a market capitalization-weighted index of the 500 widely held stocks often used as a proxy for the stock market. S&P chooses the member companies for the 500 based on market size, liquidity and industry group representation.

Disclosures

In-service withdrawals can be appropriate for many individuals. There are, however, some factors to consider:

- Exceptions to the 10% additional tax – The exceptions to the additional tax for employer plan and IRA distributions are not identical. Two exceptions apply to an employer plan, but do not apply to an IRA: separation from service at or after age 55, and Qualified Domestic Relations Orders. On the other hand, IRAs provide exceptions to the additional tax for first-time home purchase and higher education, but employer plans do not.
- Net Unrealized Appreciation (NUA) tax treatment – Favorable NUA tax treatment is not available to IRAs. Therefore, if an individual has highly appreciated company stock in his or her employer-sponsored plan, rolling that stock to an IRA eliminates the ability to take advantage of NUA tax treatment.
- Creditor protection – While IRAs now have federal bankruptcy protection, they are not protected from other judgments the way that federal law (specifically ERISA) protects qualified plans.
- New contributions to the employer plan – Taking an in-service distribution may affect a client's ability to make future contributions to the employer plan.
- Loans – In the event that a 401(k) is terminated, the loan may be subject to income taxes and a 10% additional tax.
- Availability and Fees – It is important to point out that clients should check with their employer to see if they offer in-service withdrawals. Sources of information include the Plan Administrator, Summary Plan Description, or Participant Statement. Please have clients consult these sources for any possible restrictions, fees, and expenses.
- Required Minimum Distributions (RMDs) – If the client has attained age 70½ prior to Jan. 1, 2020, RMDs are required to begin at age 70½. If the client has or will be attaining age 70½ after Jan. 1, 2020, RMDs are not required to begin until age 72. Whether clients are required to begin distributions at age 70½ or 72, the first distribution can be deferred to April 1 of the year following the year in which they attain the required distribution age. For subsequent years, distributions must be taken by Dec. 31st. If the first payment is deferred to the year following the year the client reaches the required distribution age, they will have to take two distributions within the same year. If the client is a participant in an employer plan, and is not a 5% or greater owner of the sponsoring employer, RMDs must begin at the later of the required distributions age (70½ or 72), or when they retire from that employer. If the client is a 5% or greater owner of the sponsoring employer, RMDs must begin at the required distribution age (70½ or 72).