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January 2023 Special Tax Newsletter

The 4000+ page Omnibus spending bill that passed Congress and was signed into law by President Biden in December, 2022 has many implications for individual income taxes and financial planning. Most of those provisions are in a section referred to as SECURE 2.0. While it will take some time and additional guidance from Congress and the IRS to digest this mammoth bill, I wanted to provide some highlights to you as soon as I could. This is only a partial list, aimed mainly at provisions that will affect my clients. Here we go.

Required Minimum Distributions
The law increases the age for when you must start withdrawals from retirement accounts. For those who were born in 1951 through 1959, the RMD starting age increases from 72 to 73. That means that anyone born in 1950 started taking their RMD in 2022, but anyone born in 1951 will not need to take an RMD until 2024. For those who were born in 1960 or later, the RMD starting age increases to 75. To summarize the changes:

- Those born before 1951: continue with their RMDs as normal.
- Those born 1951-1959: RMD starting age is now 73
- Those born 1960 or later: RMD starting age is now 75

What are the implications of this? For most Americans who begin drawing from their retirement accounts when they retire, nothing. But for clients who do not need to withdraw from their retirement accounts for support, it provides additional years for potential Roth conversions. Bottom line, if you turn 72 in 2023, you do not need to take an RMD until 2024 when you turn 73.

Roth 401k, 403b, and 457b Account Required Minimum Distributions (RMD)
While there have never been RMDs required on Roth IRAs, that has not been the case for employer Roth 401k/403b/457b accounts. Those accounts DID have an RMD requirement but will no longer. This provision is effective in 2024.

IRA Catch-up Limit
The IRA catch-up contribution for those over age 50 has been fixed at $1,000 for years. Effective beginning in 2024, the catch-up contribution will be indexed for inflation. Thus, we will start to see IRA catch-up contribution limits in increments of $100 for those over age 50.

Employer Plan Catch-up Limits for Certain Employees
The catch-up contribution for those over age 50 for 401k/403b plans is currently $7,500 for 2023. Thus, an employee who is age 50 or older during 2023 can contribute a total of $30,000 ($22,500 regular contribution plus $7,500 catch-up contribution) to a 401k or 403b in 2023. Effective in 2025, the catch-up contribution will increase to the greater of $10,000 or an indexed amount (which is currently higher) but ONLY for wage earners who are 60, 61, 62 or 63 during the year in question.

Employer Contributions Now Eligible for Roth Treatment
Employers will now be permitted (but not required) to deposit matching and/or other non-elective contributions into an employee's Roth account, rather than into the pre-tax account. This would generate additional income to the employee at the time of the deposit, but would make those contributions tax-free in the future. This provision is effective immediately, but will take some time for employers to adopt, if they choose to do so.

High Wage Earners MUST Use the Roth Option for Catch-up Contributions
The new law REQUIRES that catch-up contributions go into a Roth account for taxpayers whose wages for the **prior year** exceed $145,000. This provision is effective in 2024.
Thus, a wage earner who earned more than $145,000 in 2023, and is over age 50 in 2024, can contribute (based on 2023 limits) $22,500 to a 401k or 403b on a pre-tax basis, but the additional $7,500 catch-up contribution must be contributed on a Roth basis. Thus, the catch-up contribution will be taxable to the employee, but future earnings will be tax free. If the employer plan does not offer a Roth option, then this employee cannot make a catch-up contribution for that year.

529 Plan to Roth IRA Transfers
Effective in 2024, funds can be moved DIRECTLY from some 529 plans to Roth IRAs if the beneficiary of the 529 plan and the Roth IRA are the same. This provision is intended to encourage parents to save for their children's education without fear of overfunding. There are some additional limitations on this provision, such as:

- The beneficiary must have earned income (essentially wages.)
- The 529 plan account must have been maintained for 15 years or longer.
- Any contributions to the 529 plan in the prior 5 years are ineligible for transfer.
- The annual Roth IRA contribution limits apply. Thus, the most you could transfer in any given year is $6,500 (beneficiary under age 50) or $7,500 (beneficiary age 50 or older), based on the 2023 contribution limits.
- The maximum lifetime transfer is $35,000.

What Was NOT in SECURE 2.0
To the surprise of many, the following changes are not included in SECURE 2.0:

- There are no limits on the use of the Back-Door Roth or Mega-Back-Door Roth contributions.
- There are no additional income limits on who can make Roth conversions.
- The age for starting Qualified Charitable Distributions (QCDs) remains at 70 ½, despite the increase in age to start RMDs.

Again, this is only a small and partial list of the changes made by the SECURE 2.0 provisions of the Omnibus spending bill. Most of the provisions are not effective until 2024 or later, giving us some time to plan.

I will begin to address the planning related to these changes in upcoming meetings with clients.

With that, I wish you a Happy New Year!

Eric
Eric S. Korbitz CPA/PFS, CFP®
Korbitz Financial Planning LLC