The new tax law and your IRAs

The tax compromise reached by Congress and the President in December had explicit and implicit effects on planning for your IRA.

Charitable gifts from IRAs. To encourage philanthropy, Congress has for several years permitted the direct, tax-free transfer of funds from an IRA to a charity. From a tax and financial planning perspective, direct transfers are more advantageous than the alternative, which would be a taxable IRA distribution followed by a charitable gift and an income tax deduction. The strategy is limited to account owners older than 70 ½ and to $100,000 per year. Such charitable gifts also satisfy the required minimum distribution rules for older IRA owners. However, the enabling provisions expired at the end of 2009. The new tax law breathed temporary life into this strategy for tax years 2010 and 2011. Why not allow charitable gifts from IRAs permanently? Apparently, the theoretical loss of tax revenue is too high in 2012 and later years.

Roth IRA conversions. The rules for converting an IRA to a Roth IRA are unchanged. There are no income or filing status limitations on who may do this. Also, anyone who converted to a Roth IRA in 2010 has the option of paying the income tax on the conversion in full for 2010 or splitting the income over two years, 2011 and 2012, deferring the income tax and having the use of that money.

Before the tax law change, some taxpayers were favoring locking in the relatively lower 2010 tax rates by paying for the conversion with their 2010 returns. Now that the scheduled tax increase has been delayed to 2012, the math may work out differently. Deferral of the income tax may prove more valuable in some cases.

These are fairly sophisticated, complicated tax strategies. Before making any final decisions about your IRA, we recommend that you first seek the counsel of an experienced tax professional.

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