CAPTRUST

Client Conversations â?? Summer 2020

In this issue, VESTED *explores what opportunities a holiday from required minimum distributions presents to retirees in 2020, a few planning ideas to consider during market declines, and what readers should know about their chances of getting audited by the Internal Revenue Service.*

Q: Iâ??ve heard that I am not required to make withdrawals from my retirement account this year. Why is that, and what does this mean for me?

A: Youâ??re probably referring to a provision in the Coronavirus Aid, Relief, and Economic Security (CARES) Act thatâ??s been in the news. The CARES Act is the $2 trillion stimulus package passed by Congress and signed into law by President Trump in March to help alleviate financial pressures resulting from the COVID-19 pandemic.

This provision waives required minimum distributions (RMDs) from defined contribution plans, including 401(k), 403(b), and 457(b) plans, and individual retirement accounts (IRAs) for calendar year 2020. This waiver also includes RMDs from both inherited Roth and traditional IRAs.

RMDs are Internal Revenue Service-mandated distributions from retirement accounts for people 72 and older. The starting age for RMDs was raised from 70 1/2 to 72 thanks to the SECURE Act, a piece of legislation that passed in late 2019. Regardless, the IRS rules require withdrawals based upon life expectancy to ensure that these accounts are depleted as the account holder ages. The distributions are taxable as ordinary income.

The good news is that, at least for 2020, if you donâ??t need money from your retirement account, you arenâ??t required to take a withdrawalâ??and wonâ??t incur taxes on the withdrawal amount. If you are set up on a monthly distribution schedule, you may want to stop or reduce your payments so that you wonâ??t owe unnecessary taxes.

As always, new tax rules create tax-planning opportunities.

Here are few quick examples:

- Usually, an RMD cannot be rolled over or converted to a Roth IRA where it benefits from tax-free growth (and no future mandatory distributions). However, since the CARES Act waived 2020 RMDs, any RMD already taken is no longer considered an RMD. That means it can be rolled over into a Roth IRA.
- If you turned 70 1/2 last year and you were required to take your first RMD on April 1, 2020, any 2019 RMD amount not already withdrawn by January 1, 2020, is waived and you can return or roll over the RMD back into the retirement account to avoid taxation for 2020.

In both cases, there are finer point, caveats, and restrictions to consider. These things can get confusing quickly, but the tax planning opportunities can be meaningful and might be something you want to consider.

New tax rulesâ??even temporary onesâ??take time to digest and often require further clarification from the IRS. Thatâ??s certainly the case here. Thatâ??s just one more reason to make sure that you speak with your tax and financial advisors and view these opportunities through the lens of your unique financial situation.

Q: What kind of financial planning decisions should I be thinking about with the markets down?

A: It is normal to worry about personal finances after a sudden downturn in the market. Volatile markets are never easy to endure, but expecting volatility and putting a sound financial strategy in place is the best defense when things get rocky. Part of coping with market volatility is taking advantage of market downturns, because they can also create opportunity.

Understanding that every investorâ??s financial situation is unique, we firmly believe that the best strategy for most is to stay the course. But there are a few silver linings to stock market declines that are worth commenting on.

- **Tax loss harvesting.** The practice of selling an investment for a loss, tax loss harvesting is a strategy that takes advantage of temporary declines in taxable investment accounts to offset future tax liabilities. By realizingâ??or harvestingâ??a loss, investors can offset taxes on gains. When clients have significant financial life events that create capital gains, such as the sale of a business or appreciated property, tax loss harvesting can be particularly beneficial.
- **Rebalancing.** An investment accountâ??s asset allocation can be distorted by sharp moves in financial markets like the ones we have seen over the past few months. Periodic rebalancing during these declines provides an opportunity to get an account back on its target asset allocationâ??selling outperforming asset classes to buy underperforming asset classesâ??and add to solid, long-term investments that are trading at discounts to recent prices.
- **Roth conversion.** The recent market decline also makes now a good time to consider converting a portion of a traditional individual retirement account (IRA) to a Roth account to take

advantage of benefits, including tax-free income and no required minimum distribution. While you will pay taxes on the converted amount, lower account values mean that you can convert a larger portion of your account for the same tax amount to take advantage of the eventual market rebound.

While market declines are not something anyone looks forward to, a few smart moves when they happen can make a positive difference for long-term investors. Every investorâ??s situation is unique, so youâ??ll want to discuss these or any other planning ideas you are considering with your tax and financial advisors.

Q: Are some tax returns more likely to be audited than others? What happens if I get audited?

A: Being an honest taxpayer might not be enough to protect you from an audit by the Internal Revenue Service. Several factors can lead the IRS to single out your return for an audit, including having higher income. Even if you follow all the rules, a return reporting income of $200,000 or more has an increased chance of getting flagged. The same goes for taxpayers who are self-employed or run cash-intensive businesses. The IRS may also pay more attention to professionals such as doctors, lawyers, and accountants, who often run their own businesses and do their own bookkeeping.

Since 2017â??s Tax Cuts and Jobs Act, most people take the standard deduction. However, if you are one of the few people still itemizing and your medical and dental expenses, taxes, charitable contributions, and miscellaneous deductions are greater than the statistical average, you might want to arm yourself with information so you understand what the audit process is all about, why your return could be audited, and what your rights and responsibilities are.

You can either agree or disagree with the auditorâ??s findings. If you agree, youâ??ll complete some paperwork and pay whatâ??s owed (and maybe some penalties and interest).

If you disagree with the auditor, the issues in question can be reviewed informally with the auditorâ??s supervisor, or you can appeal to the IRS Appeals Office, which is independent of the local office that conducted the audit. You can appeal the auditorâ??s findings by sending a protest letter to the IRS within 30 days of receiving the audit report. If you do not reach an agreement with the appeals officer (or you do not wish to use the appeals office), you may be able to take your case to the U.S. Tax Court, U.S. Court of Federal Claims, or U.S. District Court where you live.

First and foremost, you can help protect yourself against an IRS audit by ensuring that your tax return is not missing required schedules or forms, that your records clearly substantiate the items claimed on your return, and that your return is not signed by a preparer associated with problems in the past.

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