Understanding **IRA distributions**

A retirement distribution guide

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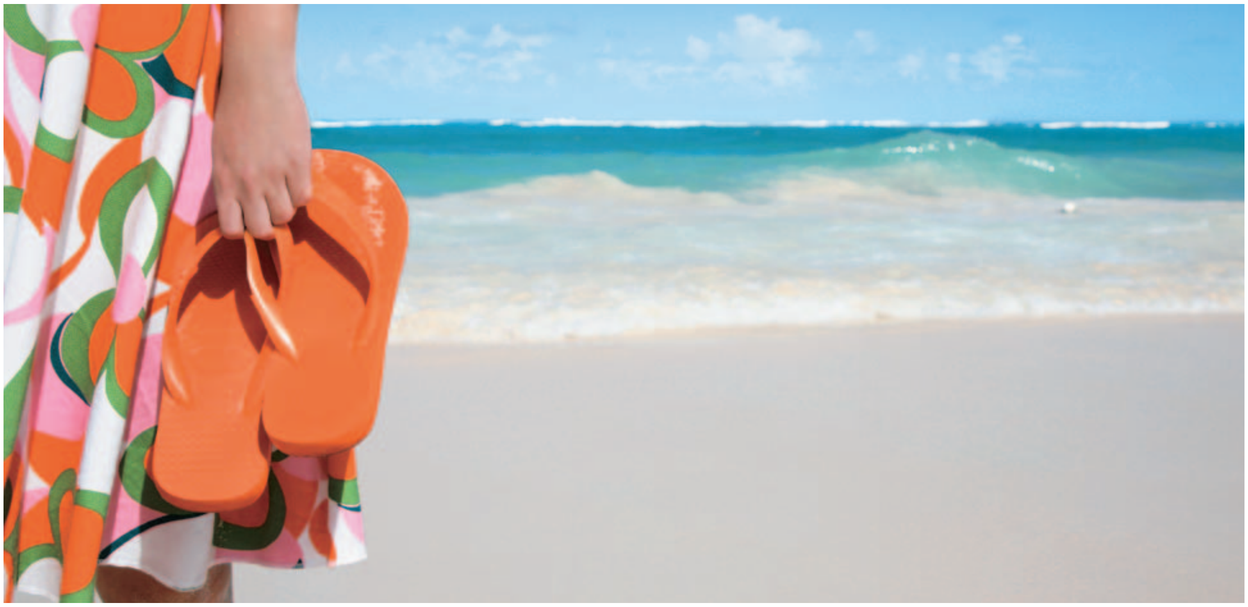

It’s important to know how much you need to save for retirement. But it’s just as important to have a strategy for taking your retirement income.

In this guide, we’ll look at some of the factors you should consider as you develop a distribution strategy for your individual retirement arrangement (IRA):

- We’ll explore some of the taxation basics of IRAs.
- We’ll look at the role your age plays in taking distributions from your IRA.
- We’ll also see why it’s important to carefully consider your beneficiaries.

Any transaction that involves a recommendation to liquidate funds held in a securities product, including those within an IRA, 401(k), or other retirement plan, for the purchase of an annuity, can be conducted only by individuals currently affiliated with a properly registered broker/dealer or registered investment advisor. If your financial professional does not hold the appropriate registration, please consult with your own broker/dealer representative or registered investment advisor for guidance on your securities holdings.

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Purchasing an annuity within a retirement plan that provides tax deferral under sections of the Internal Revenue Code results in no additional tax benefit. An annuity should be used to fund a qualified plan based upon the annuity’s features other than tax deferral. All annuity features, risks, limitations, and costs should be considered prior to purchasing an annuity within a tax-qualified retirement plan.

IRA basics: traditional vs. Roth

There are important tax differences between a **TRADITIONAL** and **ROTH IRA**.

Traditional IRA

All distributions from traditional IRAs are taxed as ordinary income, except to the extent that they represent funds you did not deduct on your income tax return back when you contributed them (or were after-tax funds for some other reason).

Roth IRA

Qualified distributions from Roth IRAs are income-tax-free. Qualified distributions mean that you take your withdrawal more than five years after you first opened any Roth IRA, and you have one of these occurrences:

- Age 59½
- Disability
- Death
- First-time home purchase (up to $10,000 lifetime limit)

If you fail to wait five years or you don't have one of these occurrences, distributions of earnings from your Roth will be taxed as ordinary income. However, Uncle Sam deems that the first monies you withdraw are your Roth contributions and conversions, which come out income-tax-free (you already paid tax on them). This includes conversions done by rollover from an employer retirement plan to a Roth IRA. The portion of distributions deemed to be conversions may be subject to the 10% federal additional tax for early distribution if you are under age 59½ and the distribution is taken within five years of the conversion.

Early distributions and the 10% federal additional tax

Traditional IRA

Congress designed IRAs to encourage saving for retirement. The Internal Revenue Code therefore imposes a 10% federal additional tax for withdrawing IRA funds prior to age 59½. This is in addition to the income taxes due. There are some situations in which you can withdraw from an IRA before age 59½ without owing a 10% federal additional tax. The exceptions to the 10% federal additional tax may include the following, but this is not intended to be a complete list:

- Death
- Disability
- First-time home purchase (up to $10,000 lifetime limit)
- Certain deductible medical expenses
- Qualified education expenses for you, your spouse, child, or grandchild
- Health insurance premiums if you're unemployed

Allowable distributions before age 59½

You **CAN RECEIVE** distributions prior to age 59½, without incurring federal additional tax, but certain rules must be followed.

If you need income prior to age 59½ , you can also avoid the 10% federal additional tax by taking distributions from your IRA in substantially equal periodic payments over your life expectancy. Once you start these payments, you cannot modify this stream of income until you are age 59½ and the five-year period starting with the date of the first payment has passed.

"Modification" not only includes changing the payment, but also adding or withdrawing additional funds from the IRA (although you could add to other IRAs). If you do modify the stream of payments, you will have to pay the 10% federal additional tax retroactively on all distributions that you received prior to age 59½, plus interest for the deferral period.

Many IRA providers will calculate a substantially equal periodic payment stream for you and indicate to the IRS on your annual Form 1099R that you fall under an exception to the 10% federal additional tax. However, you can report the exception to the 10% federal additional tax yourself on IRS Form 5329, which would be filed with your annual tax return.

Roth IRA

If you take a taxable distribution of earnings from a Roth IRA or a nonqualified distribution of conversion amounts within five years of their deposit into the Roth IRA, you are also subject to the 10% federal additional tax if you're under age 59½. You may be able to avoid the federal additional tax if any of the exceptions previously noted for traditional IRAs on page 1 apply.

If you need additional income before age 59½, discuss your options with your financial professional.

Hypothetical example of substantially equal periodic payments

Jake is 52 years old and retiring. He wants to take income from his IRA yet still avoid the 10% federal additional tax for pre-age 59½ withdrawals. Under IRS rules, Jake can avoid this by taking substantially equal periodic payments over his life expectancy.

The IRS sanctions three methods for figuring substantially equal periodic payments: the annuitization method, the amortization method (also called the required minimum distribution (RMD) method), and the life expectancy method. The annuitization and amortization methods set a flat dollar amount to withdraw each year. The life expectancy method, as described on page 5, is figured similarly to the required minimum distributions (RMDs). Such a payment will typically start small and get larger each year.

Assuming that Jake has $300,000 in his IRA and the hypothetical reasonable interest rate is 1.53%, based on 120% Applicable Federal Rates (AFR) for annual payments, Jake's equal payment can be:

Annuitization method:	$11,765
Amortization method:	$11,840
Life expectancy method:	$ 9,287

Jake wants the highest payout, so he chooses the $11,840 payment of the amortization method. He takes $11,840 each year. Jake can modify the payment after the later of five years (the five-year period starting with the date of the first payment) or age 59½.

Please note: This is an example only. Before requesting substantially equal periodic payments, you should consult your tax advisor to determine what interest rate and other assumptions should be used to calculate the appropriate payment amount in your specific situation.

Regular traditional IRA distributions

Between ages 59½ and 70½, you can withdraw as much or as little from your traditional IRA as you deem prudent without a 10% federal additional tax. (Regular income taxes will apply, as described previously.) If the IRA is an annuity, contract restrictions and surrender charges may apply.

Distributions after age 70½

Roth IRA

If you have a Roth IRA, you are not required to take any distributions from your Roth IRA during your life. Your beneficiaries, though, will have to take required minimum distributions after your death (refer to page 5).

REQUIRED DISTRIBUTIONS may or may not apply depending on if you have a Roth or traditional IRA.

Traditional IRA

If you have a traditional IRA, you must begin to take at least the required minimum distribution at age 70½ (we will discuss what a required minimum distribution is on page 4). If you take less than the required minimum distribution, you will be assessed a 50% penalty on the amount you should have taken, but failed to take.

While there is a minimum you are required to withdraw after age 70½, there is no maximum. In any year, you can take any amount over the RMD. However, the tax deferral that the IRA provides is valuable, and you may want to preserve it through your life and even pass it on to your heirs after you die (see the distribution strategies on page 8). Your financial and tax professionals can help you choose among all your sources of retirement income for the most tax-efficient strategy.

Mandatory distributions

For traditional IRAs, you must take at least a required minimum distribution (RMD) for the year you turn age 70½ and each year thereafter. However, the distribution for the first year can be delayed until your required beginning date. The required beginning date for your traditional IRA is April 1 of the year after the year you turn age 70½. In every other year, you must take a withdrawal by December 31. Note that if you delay your first distribution until April 1 of the year after age 70½, you will have to take two distributions in that year. Consider how two payments in the same year could affect your income taxes.

Calculating the RMD

As we've just seen, you must take an RMD from a traditional IRA for the year you turn age 70½ and each year thereafter. After your death, your beneficiaries will also be required to take at least a minimum distribution.

For simplification, let's assume that you have an IRA from which an RMD must be taken. For any given year, you find the value of the IRA on December 31 of the prior year and divide it by the remaining life expectancy, based on IRS tables, of the person entitled to the funds (i.e., you the owner or, after your death, your beneficiary). In certain circumstances, the life expectancy of the deceased is used instead of the life expectancy of the person entitled to the funds. The resulting figure is the required minimum distribution amount that must be taken during the year to avoid the 50% penalty. If you have more than one IRA, each IRA will also have an RMD computed in the same manner. (Different rules apply to annuitized IRAs.)

Both **YOU** (after age 70½) and/or **YOUR BENEFICIARIES** (after your death) will be REQUIRED to take a minimum distribution.

See your financial and tax professionals for options concerning where the funds can be drawn from to satisfy your total RMD obligation. For example, you can aggregate non-annuitized IRAs and take an RMD (surrender charges may apply) from just one IRA. If your IRA is funded with a deferred annuity, a special RMD calculation may apply.

In addition, special RMD rules may apply if an IRA owner annuitizes their contract. In general, each annuity payment from the IRA is required minimum distribution, regardless of the age of the IRA owner or beneficiary and of the length of any guarantee period. See your tax advisor.

IRA providers are required to do the RMD calculation for you, if you wish. Providers will only calculate RMDs for amounts held with them. This may be a good idea if the IRA is an annuity because IRS regulations define the December 31 value. The December 31 value for an annuity is now the IRA cash value plus, for many annuities, the actuarial present value of other living benefits and death benefits.

Hypothetical RMD calculation

Alyshia wants to take an RMD for 2012. The value of her IRA was $100,000 on December 31, 2011. Alyshia turns 74 years old on her birthday in 2012. According to the Uniform Table, the life expectancy for a 74 year old is 23.8 years. Alyshia's RMD for 2012 is $100,000 divided by 23.8; therefore, $4,201.68. This is her required minimum distribution to avoid the 50% penalty. Alyshia can take more than this amount if she wishes.

The RMD regulations also tell us what life expectancy to use, based on whom the IRA benefits. While you're alive, the life expectancy is found either on the Uniform Table or the Joint Life Table. Most IRA owners use the Uniform Table. The Uniform Table assumes, whether true or not, that you are taking distributions over your joint life expectancy with a beneficiary who is 10 years younger. This assumption benefits you because it gives you a longer life expectancy and thus requires a smaller percentage payout. To use the table, look up your age based on how old you will be on your birthday in that year. The Uniform Lifetime Table is printed on page 9.

Other calculation methods

If your spouse is your sole beneficiary and is more than 10 years younger than you, you can use your joint life expectancy found on the Joint Life Table of IRS Publication 590. This will be a longer life expectancy than the Uniform Table, so required distributions will be smaller. Again, you may want to have the provider calculate the RMD for the year.

Life expectancy

As a traditional IRA owner, your life expectancy is recalculated each year you're alive. That is, you look up your life expectancy on the table each year. Even from age 115 on, you are assumed to have a 1.9-year life expectancy. By recalculating, you will never run out of life expectancy.

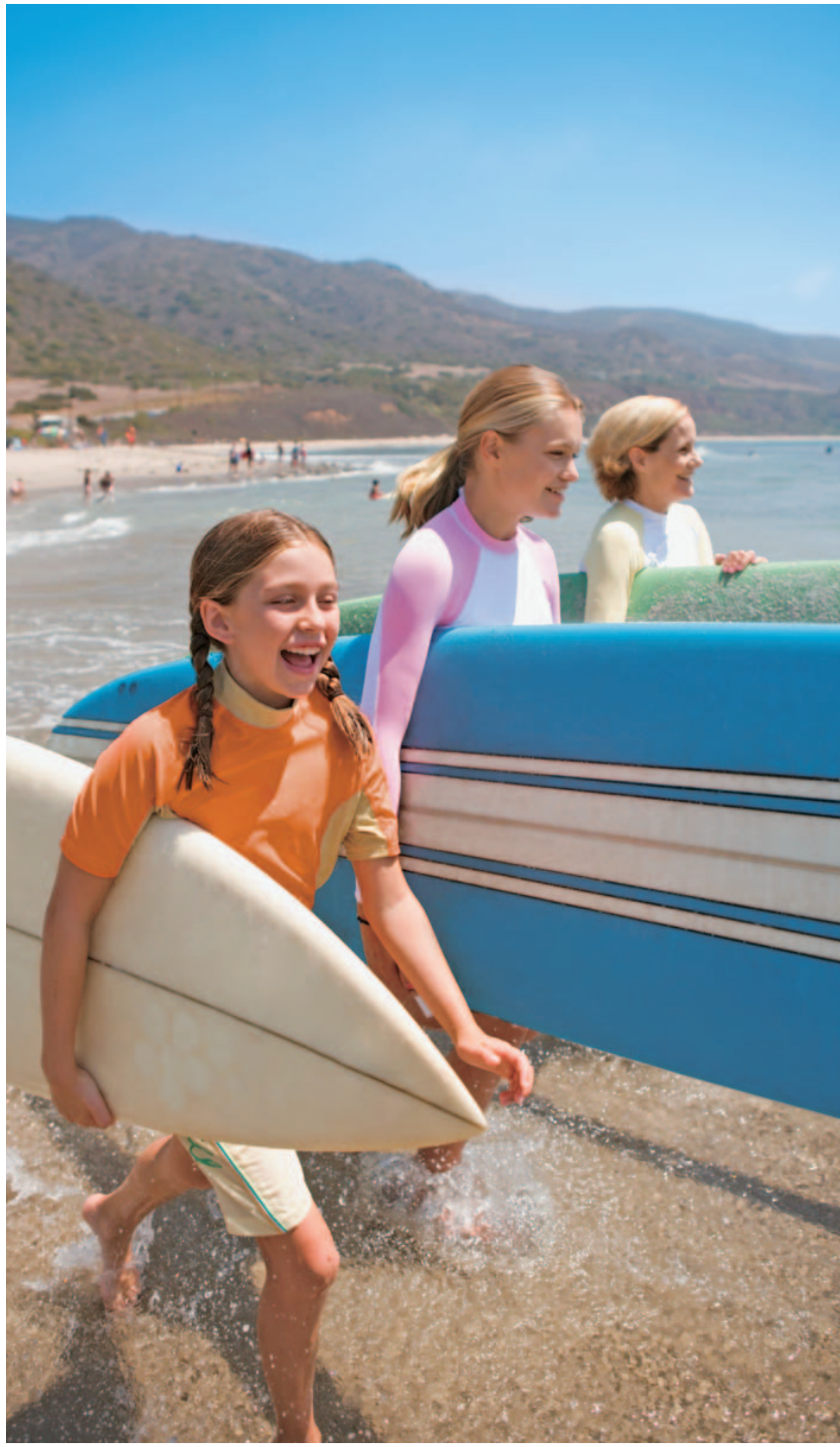
As each year goes by, your life expectancy will shorten (until age 115) and distributions will become a larger percent of the IRA balance. However, by taking no more than the required minimum distribution, you may still be able to preserve a large balance in this IRA for your beneficiaries.

Distribution in the year of death

If you are over age 70½ and must take an RMD for the year, but die before the withdrawal, your beneficiary must take your RMD before December 31 of the year you die.

Distribution options after death

Beneficiaries of both traditional IRAs and Roth IRAs must take distributions after your death. IRS regulations offer the beneficiary several options for taking distributions. The options vary depending on 1) whether the beneficiary is a spouse, nonspouse, or there is no "designated beneficiary" (which usually means the beneficiary is an entity such as a charity or an estate), and 2) whether you die before or after your required beginning date (i.e., April 1 of the year after the year you turn age 70½). Check with your IRA provider regarding the specific rules.



Naming a beneficiary

ALLOCATION OPTIONS **CHANGE** based on the beneficiary you choose.

Spouse beneficiary

If you name your spouse as beneficiary of your traditional or Roth IRA, your spouse has the following options if you die **before** your required beginning date:

- Lump sum
- Defer distribution for now, as long as the IRA is emptied by December 31 after the fifth anniversary of the death ("5-year deferral").
- RMDs over spouse's single life expectancy (using the Single Life Table – which has shorter life expectancies than the Uniform Lifetime Table – see page 9). Payments begin by December 31 of the year after the owner dies. During life, a spouse can recalculate the life expectancy each year. When a spouse dies, the life expectancy figure becomes "fixed" at that point. This means that from then on, the life expectancy figure drops one year for each year that passes, as far as the spouse's beneficiaries of that IRA are concerned. The beneficiaries of the now-deceased spouse can ride out this fixed term but cannot extend for another life expectancy.
- Defer distribution for now, but take RMDs using spouse's single life expectancy beginning when you would have turned age 70½.
- Roll over or continue the IRA in his or her own name. As the spouse becomes the new owner, the RMD rules are reset: The spouse can wait to take RMDs until the spouse's own age 70½ as described above.

A spouse beneficiary of your traditional or Roth IRA has the following options if you die on or **after** your required beginning date:

- Lump sum
- RMDs over spouse's single recalculated life expectancy, or over your remaining single fixed life expectancy, whichever results in smaller distribution
- Roll over or continue the IRA in his or her own name

Many spouses will want to roll over the funds to their own IRA. Spouses who are under age 59½ might not want to roll their inherited traditional IRA over to their own IRA if they need to withdraw funds from the IRA for their support. That's because if they rolled over and became owners, they would lose the death benefit payment penalty exception, and it would be subject to the 10% federal additional tax for premature distributions. After they reach age 59½ and are no longer subject to the 10% federal additional tax for premature distributions, they can roll over the IRA to their own name and take distributions or defer as they wish. The 10% federal additional tax is only a concern with the rollover (continuation) option. Spouse beneficiaries of Roth IRA funds will want to consider how rolling over the funds to their own Roth IRA will affect their ability to receive qualified distributions of the funds. It is possible that rolling over and then distributing could cause the distributions to be subject to both income and penalty taxes. Spouses also might not want to roll their inherited traditional IRA over to their own IRA if the RMD from the inherited IRA would be less than the RMD from their own IRA.

Nonspouse beneficiary

A nonspouse beneficiary (child, grandchild, sibling, partner, etc.) has the following options if you die **before** your required beginning date:

- Lump sum
- 5-year deferral
- RMDs over the beneficiary's single fixed life expectancy. Unlike a spouse, the beneficiary's life expectancy is fixed, not recalculated. You look up the beneficiary's life expectancy on the Single Life Table (refer to page 9) once in the year after death, and reduced by one year as each year passes. If the beneficiary dies before the term is up, his or her beneficiaries can ride out the rest of the term.

A nonspouse beneficiary has the following options if you die on or **after** your required beginning date:

- Lump sum
- RMDs over their fixed single life expectancy, or over your fixed single life expectancy, whichever results in the smaller amount

Some things to keep in mind:

- If a beneficiary chooses to take RMDs (that is, does not choose one of the deferral options), they must make the first withdrawal by December 31 of the year after the year you die, and at least annually thereafter. As noted above, a spouse beneficiary may be able to defer longer before starting RMDs.
- If you name more than one beneficiary on your IRA, the beneficiaries will have until September 30 of the year after your death to divide the IRA into separate shares, one for each beneficiary. After that, each beneficiary can choose among their options as he or she wishes, and if they choose to take RMDs, they can use their own life expectancy.
- If you want to designate a minor as beneficiary of your IRA, you should consider naming a trust or custodian under their state Uniform Gifts for Minors Act or Uniform Transfer to Minors Act (UGMA/UTMA). Many state laws forbid an insurance company from paying funds to a minor directly.
- If you name a trust as the beneficiary of the IRA, the trust can take RMDs over the life expectancy of the oldest trust beneficiary provided that all the beneficiaries are persons and that these rules are met:
  - The trust is valid under state law.
  - The trust is irrevocable or becomes irrevocable at your death.
  - The trust beneficiaries are all individuals and are identifiable.
  - You or the trustee give the IRA provider a copy of the trust or documentation showing the IRA provider the necessary information on beneficiaries by a certain time.

If these requirements are met, a trust beneficiary can take RMDs over the fixed life expectancy of the oldest trust beneficiary. The trustee will pass out those funds to the beneficiaries or accumulate them as the trust terms dictate.

No designated beneficiary

If you do not name a beneficiary and the IRA does not have a default to a spouse or nonspouse, or if that beneficiary is a non-natural entity such as an estate, charity, or corporation, the inheritor has the following options if you die **before** your required beginning date:

- Lump sum
- 5-year deferral

A non-natural beneficiary has the following options if you die on or **after** your required beginning date:

- Lump sum
- RMDs over your remaining fixed actuarial life expectancy

Note that if you fail to name a beneficiary, the estate will, by default, be the beneficiary unless there are default provisions in the IRA specifying a different default beneficiary.

Distribution strategies

A **SOLID DISTRIBUTION STRATEGY** CAN HELP YOU MEET YOUR RETIREMENT GOALS.

Here are some examples of distribution strategies or parts of distribution strategies. Ask your financial or tax professional if these, or other strategies not identified here, might be good for you, your income, and your tax situation:

- Before age 59½, use non-IRA funds for your income to avoid the 10% federal additional tax.
- If you need income from your IRA before age 59½, substantially equal periodic payments are an option to avoid the 10% federal additional tax and provide a bridge until you start receiving Social Security and/or other pension income. After the end of the five-year period starting with the date the first payment is made and attaining age 59½, if you no longer need all the IRA funds, reduce the stream of income until the rules say you must take RMDs at age 70½.
- After age 70½, you can aggregate all your non-annuitized IRAs and figure an RMD amount on the total value. You can take this RMD value from just one or a few IRAs if you wish. However, surrender charges may apply if early withdrawals are taken from an annuity.
- Reduce your taxable income by mixing taxable traditional IRA distributions with tax-free Roth IRA qualified distributions.
- Take just required minimum distributions from your traditional IRA to keep income taxes down, perhaps reduce taxes on Social Security benefits, and preserve the tax deferral of the IRA for your beneficiaries.
- Choose younger beneficiaries so that after your death, they can stretch the traditional or Roth IRA distributions over their life expectancies if they choose. Their required distributions may be so small at first that the IRA earnings may outpace the distributions, allowing the IRA to continue to grow for some time after your death.
- Avoid lifetime distributions from your Roth IRA, if you can afford it, to preserve tax-free qualified distributions for your beneficiaries.
- Discuss with your tax professional whether spending traditional IRA funds during retirement will help to avoid selling low-basis capital gain property. Depending on estate tax rules at the time of your death, capital gain property may have its basis stepped-up at death, up to that point. Gains from that point forward would be taxable. In contrast, traditional IRA distributions will be taxed as ordinary income to your beneficiaries, although they may spread the taxation by receiving RMD payments based on their life expectancies.
- If you have both a traditional IRA and a Roth IRA and you want to designate a charity as a beneficiary, consider naming the charity as beneficiary on the traditional IRA instead of the Roth IRA since qualified Roth IRA distributions are income-tax-free to any beneficiary.

A sound retirement income strategy

A critical step to your long-term financial well-being. As we've seen, there are several factors to take into account as you develop a distribution strategy for your traditional or Roth IRA. Work with your financial or tax professional to determine which strategy or strategies will best meet your needs.

This material is for informational purposes only. It should not be considered an offer of any tax plan or arrangement. You can use a variety of funding vehicles to plan for your retirement. You should consult your financial and tax professionals to help you determine what is most suitable for your individual needs.

Uniform lifetime table[1]

For use by all owners during life, unless the sole beneficiary is a spouse who is more than 10 years younger than the owner. In that case, please refer to the Joint Life Table from IRS Publication 590, Appendix C.

Age	Distribution period	Age	Distribution period	Age	Distribution period	Age	Distribution period
70	27.4	82	17.1	94	9.1	106	4.2
71	26.5	83	16.3	95	8.6	107	3.9
72	25.6	84	15.5	96	8.1	108	3.7
73	24.7	85	14.8	97	7.6	109	3.4
74	23.8	86	14.1	98	7.1	110	3.1
75	22.9	87	13.4	99	6.7	111	2.9
76	22.0	88	12.7	100	6.3	112	2.6
77	21.2	89	12.0	101	5.9	113	2.4
78	20.3	90	11.4	102	5.5	114	2.1
79	19.5	91	10.8	103	5.2	115 an over	1.9
80	18.7	92	10.2	104	4.9		
81	17.9	93	9.6	105	4.5		

Single life expectancy table[1]

For use by beneficiaries after the owner's death.

Age	Distribution period	Age	Distribution period	Age	Distribution period	Age	Distribution period
0	82.4	28	55.3	56	28.7	84	8.1
1	81.6	29	54.3	57	27.9	85	7.6
2	80.6	30	53.3	58	27.0	86	7.1
3	79.7	31	52.4	59	26.1	87	6.7
4	78.7	32	51.4	60	25.2	88	6.3
5	77.7	33	50.4	61	24.4	89	5.9
6	76.7	34	49.4	62	23.5	90	5.5
7	75.8	35	48.5	63	22.7	91	5.2
8	74.8	36	47.5	64	21.8	92	4.9
9	73.8	37	46.5	65	21.0	93	4.6
10	72.8	38	45.6	66	20.2	94	4.3
11	71.8	39	44.6	67	19.4	95	4.1
12	70.8	40	43.6	68	18.6	96	3.8
13	69.9	41	42.7	69	17.8	97	3.6
14	68.9	42	41.7	70	17.0	98	3.4
15	67.9	43	40.7	71	16.3	99	3.1
16	66.9	44	39.8	72	15.5	100	2.9
17	66.0	45	38.8	73	14.8	101	2.7
18	65.0	46	37.9	74	14.1	102	2.5
19	64.0	47	37.0	75	13.4	103	2.3
20	63.0	48	36.0	76	12.7	104	2.1
21	62.1	49	35.1	77	12.1	105	1.9
22	61.1	50	34.2	78	11.4	106	1.7
23	60.1	51	33.3	79	10.8	107	1.5
24	59.1	52	32.3	80	10.2	108	1.4
25	58.2	53	31.4	81	9.7	109	1.2
26	57.2	54	30.5	82	9.1	110	1.1
27	56.2	55	29.6	83	8.6	111 and over	1.0

[1] 2011 IRS Publication 590, Appendix C.

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