



# 2023 TAX-SMART IRA STRATEGIES



## INTRODUCTION

A self-directed IRA is one of the most versatile and tax-smart wealth accumulation vehicles available today. When you save in a taxable account, the investment growth — such as interest and dividends — is taxable each year. When you save in an IRA, investment growth is sheltered from taxation while the asset is held in the IRA. This helps reduce your taxable income in the years leading up to retirement. Depending on the type of IRA you choose, an IRA can also allow you to:

- Reduce your taxable income today with tax-deductible contributions.
- Pay tax at today's rates on your retirement savings.
- Pay tax on your retirement savings at any time in the future, including before retirement.
- Grow your investments in a tax-free environment.
- Create investment and withdrawal strategies to manage your tax liability in retirement.
- Leave tax-free wealth for heirs.

Figure 1: 2022 & 2023 Contribution Limits

Annual Contribution Limits	2022	2023	Catch-Up Contribution Limit For Age 50 And Older
Traditional & Roth IRAs (in aggregate)	\$6,000	\$6,500	Additional \$1,000

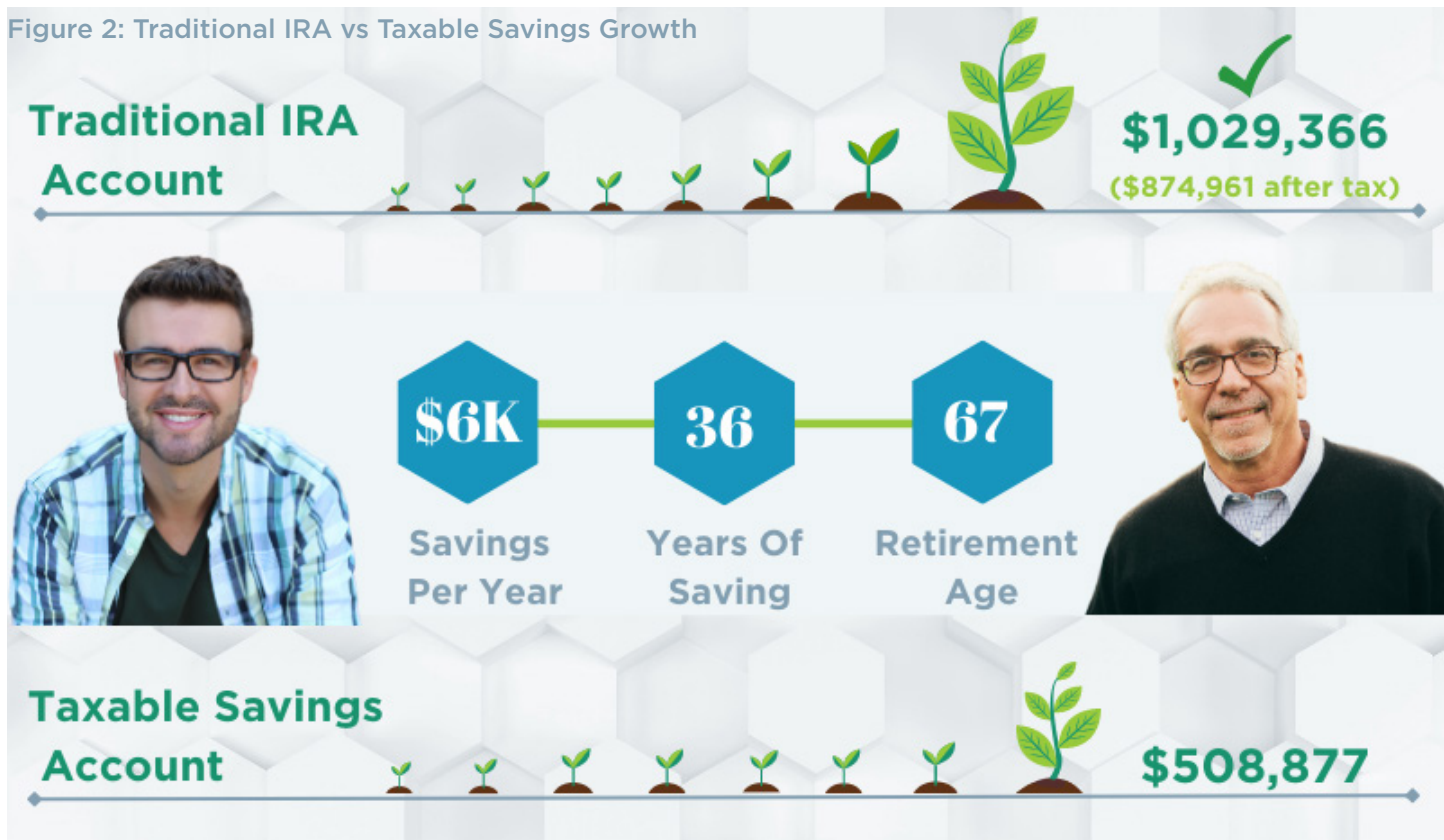
The maximum permitted contribution to a tax-advantaged retirement savings account each year is adjusted annually relative to the cost-of-living index (Figure 1). As the cost of living goes up, so too do the contribution limits. For 2023, the IRA contribution limits will be increasing, as will the income limits that determine who can take a tax deduction for a Traditional IRA contribution and who can contribute to a Roth IRA. This means more taxpayers will be permitted to save more in an IRA in 2023.



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Additionally, when and how taxes are applied to your investments can make a dramatic impact on your savings accumulations over time. For example, in Figure 2 below you can compare the hypothetical outcome of a 30-year-old investor (Jim) saving \$6,000 per year for 36 years in both a taxable account and a Traditional IRA. Assuming Jim is in a 25% income tax bracket during his working years, the taxable account contributions are calculated based on the after-tax cost of

contributing \$6,000 per year (\$4,500). Each account earns a 7% return. At age 67, Jim could have a pre-tax IRA balance worth \$1,029,366. After paying taxes in retirement (at a 15% tax rate), the IRA would be worth \$874,961. Jim's balance in the taxable account at retirement, while tax-free, would be \$508,877. Begin planning now so you can make the best use of tax-smart IRA strategies at every age.



Certain types of investments earning "unrelated business taxable income" may trigger current-year taxation inside an IRA.  
<https://www.stratatrust.com/resource-center/financial-calculators/traditional-ira-calculator/>



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## MAX OUT IRA CONTRIBUTIONS AND TAX BENEFITS

In addition to contributing the maximum amount permitted to your IRA each year, consider how you can maximize the tax benefits available for IRA contributions.

Contributions to a Traditional IRA allow you to defer paying tax on the amount you contribute and any investment growth until you withdraw funds from the IRA—typically in retirement.

Contributions to a Roth IRA are made on an after-tax basis, but you can withdraw your contributions any time tax-free, and you will never pay tax on the investment growth in your Roth IRA if you take qualified distributions (i.e., have a Roth IRA for at least five years and be age 59½ or older, disabled, deceased, or a first-time homebuyer at the time of distribution).

To determine the type of IRA and tax benefits that work best for you, think about when you want to pay tax on your IRA assets: today or in retirement.

### Pay Tax In Retirement (Traditional IRA) If You:

- Want to reduce your taxable income during your earning years
- Will have less taxable income in retirement
- Think tax rates will be lower when you retire

### Pay Tax Now (Roth IRA) If You:

- Anticipate significant investment growth in your IRA
- Will have more taxable income in retirement
- Think tax rates will be higher when you retire

A truly tax-smart IRA strategy that's right for you should depend on several factors — including your income, marital status, tax bracket, age, and the tax status of your other retirement savings. Your tax or financial advisor can help you evaluate your needs. Before making a decision, here are some IRA rules you should be aware of.<sup>3</sup>

- You can contribute to an IRA at any age, but you need earned income (typically from working) at least equal to the amount you contribute.

<sup>3</sup> For more information, see the IRS's IRA Contribution website.



- ☑ Each spouse in a married couple filing a joint tax return can contribute to their own IRA as long as one spouse has enough earned income to support both contributions.
- ☑ You can take a deduction for a Traditional IRA contribution no matter how high your income unless you (or a spouse) participate in a retirement plan at work. In this case, your modified adjusted gross income (MAGI) must be under a certain amount to qualify for a deduction.
- ☑ Contributing to an IRA does not limit how much you can contribute to a Health Savings Account (HSA) or an employer's retirement plan.
- ☑ You cannot contribute to a Roth IRA if your income exceeds a certain amount. For example, if you are married and your MAGI is more than \$228,000, you are not eligible to contribute to a Roth IRA.

### SAVE MORE IF YOU OWN YOUR OWN BUSINESS

As a business owner, you can establish an IRA-based retirement plan for your company and contribute even more to a self-directed IRA. Your plan contributions will be tax-deductible for your business.

### SIMPLIFIED EMPLOYEE PENSION (SEP) PLAN

Any type of business can establish a SEP plan, but it's most often used by sole proprietors and smaller, family-owned businesses because the business is the sole contributor to the plan. The business may contribute up to the lesser of 25% of your compensation or \$66,000 for 2023 to your Traditional IRA. Business owners can choose whether to fund the SEP plan each year, but if the business has employees and makes a SEP plan contribution for a year, each eligible employee must receive a contribution equal to the same percentage of compensation.



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## SIMPLE IRA PLAN

A SIMPLE IRA plan is a 401(k)-type plan designed solely for employers with 100 or fewer employees who earned more than \$5,000 in the preceding year. A SIMPLE IRA plan has fewer administrative responsibilities and costs for the business owner compared to a 401(k) plan, but the business must commit to a contribution each year. Eligible employees may choose to have a portion of their pay deducted from their paychecks (pre-tax) and deposited into their SIMPLE IRA – up to \$15,500 for 2023, plus a \$3,500 catch-up contribution. The business can choose to either match employees' salary deferrals up to 3% of compensation, or provide a 2% nonelective contribution to eligible employees each year.

## DIVERSIFY YOUR ASSET LOCATION

Diversifying the types of accounts that hold your investments, from a tax perspective, can be just as important to your retirement savings strategy as diversifying your investments. Although IRAs are tax-smart, taxable accounts offer certain tax benefits that may be a better fit for certain types of investments based on the type of growth expected and the tax rules for the account. For example, it can make sense to hold

equities offering the opportunity for favorable long-term capital gains treatment in a taxable account, since the long-term capital gains rate will likely be lower than your income tax rate. Qualified dividends from these holdings are also eligible for preferential tax treatment. You may also be able to use a taxable account to reduce your current year's tax bill if you can offset investment gains with investment losses realized after selling securities (tax-loss harvesting).

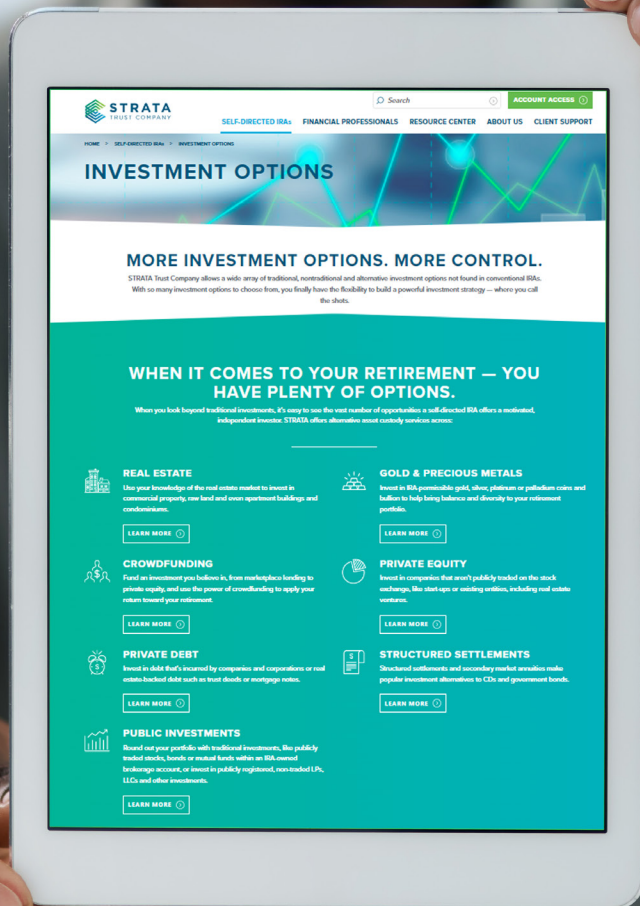
Conversely, investments that are expected to generate lower returns, like bonds, might be better held in a tax-deferred IRA. This allows you to defer taxes on this income until retirement but control the amount that will be taxable to you in retirement. Other investments, like equities with a high growth potential, could be held in a Roth IRA, where the growth will be tax-free when distributed in retirement. Asset location should also be a key consideration if you're investing in alternative assets. Many alternatives have tax implications that can be avoided or mitigated inside an IRA.

Investing in a combination of taxable, tax-deferred, and tax-free accounts now during your saving years can increase your options for withdrawals if you need to access your savings before age 59½. And when you retire, having a combination of accounts will provide you with the most flexibility for creating a tax-smart retirement income strategy; for example, using your taxable and tax-free distributions to manage your tax bracket,



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rather than carrying the full tax liability of all your savings and Social Security benefits into retirement.

**ALTERNATIVE INVESTMENTS CAN INCLUDE:**



**Venture Capital**

Pre-IPO organizations in the early stage and often showing early signs of high growth.

**Private Capital Raises**

Established organizations focusing on expansion/new technology resources.



**Infrastructure**

Purchase & ownership of physical assets such as bridges, roads, and hospitals.



## CONSIDER STRATEGIC ROTH CONVERSIONS

If tax-free income in retirement is your goal, a Roth IRA is a tax-smart saving tool. The less taxable income you have in retirement, the lower your tax bracket will be. You also may be able to reduce taxes you would otherwise have to pay on your Social Security retirement benefits and potentially on investment income if you're in a high tax bracket.

Additionally, Roth IRAs are not subject to annual required minimum distributions (RMDs), so you are never forced to liquidate an investment or withdraw from your Roth IRA. Your beneficiaries must withdraw your Roth IRA assets within a certain number of years following your death, but the assets will be tax-free for them too.

To reduce your income tax in retirement, you might consider converting some of your pre-tax retirement savings to a Roth IRA now. The amount converted must be included in your current-year taxable income (excluding any basis), but you won't have to pay tax on that amount again, and any investment growth after the conversion will be tax-free in retirement.



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## TAX-SMART CONVERSION STRATEGIES

- Conduct a series of conversions to spread the tax impact over several years.
- Consider a conversion in years when your income or tax bracket is lower than normal.
- Estimate where your income will fall within your tax bracket for the year and convert a dollar amount that will “fill up” that tax bracket without exceeding it.
- Convert investments in-kind during down markets or when the investment value is low to reduce your tax liability on the conversion and increase your potential for tax-free growth.
- Wait to convert taxable retirement savings until after you stop working full time but before you claim Social Security or are subject to RMDs. This may be a time when your taxable income is at its lowest.
- If your income makes you ineligible to contribute to a Roth IRA, consider the “back door” strategy, in which you make nondeductible contributions to a Traditional IRA, then convert them to a Roth IRA. This strategy assumes you have little or no pre-tax assets in your IRAs because you cannot withdraw or convert just nondeductible contributions. Withdrawals from a Traditional IRA consist of a pro rata portion of the taxable and nontaxable assets held in your Traditional, SEP, and SIMPLE IRAs.

While conversions allow you to choose when to pay tax on your retirement earnings, you’ll want to carefully consider the impact they can have on your tax liability for the year of conversion. For example, the increased income may bump you into a higher tax bracket or subject you to the 3.8% Medicare tax on net investment income.

## REDUCE, RE-USE, RECYCLE RMDs

Saving for retirement on a pre-tax basis in a workplace retirement plan or Traditional IRA can help lower your tax liability during your working years but can create a large tax liability for you in retirement. The tax laws require that you begin taking annual withdrawals from your pre-tax accounts when you reach age 72. These required minimum distributions (RMDs) are taxable, and you’ll face a 50% tax penalty if you miss an RMD. This added annual taxable income can negatively affect other areas of your finances, including increasing your tax bracket, your Medicare bill, and tax on your Social Security retirement benefits. Depending on your situation, one or more of the following strategies may help reduce the amount of your RMDs or tax liability, or re-invest your RMDs to continue working for you.



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**REDUCE**

Roth IRAs are not subject to age 72 RMDs. You can reduce your future RMDs by converting some of your pre-tax retirement savings to a Roth IRA.

**RE-USE**

If you're still earning an income after age 72, you could use your Traditional IRA RMD to make a Roth IRA contribution. You'll still be taxed on the distribution from your Traditional IRA, but you'll be able to re-invest the money and grow your investment tax-free. If you're not eligible to contribute to a Roth IRA, you could transfer your RMD in-kind to a taxable account, so you can continue growing your investment.

**RECYCLE**

You may avoid taxation on an RMD by making a Qualified Charitable Distribution (QCD). Because QCDs must come from pre-tax savings, the money you donate will be entirely tax-free (you did not pay tax on the money going into the IRA and you will not pay tax on the money you donate). The donation must come directly from your IRA to qualify, so be sure to request a QCD payable to an organization of your choice before your RMD is paid out for the year.



- IRA owners and beneficiaries age 70½ or older at the time of the distribution may make a QCD. No need to itemize deductions on your tax return.
- QCDs can be made from Traditional IRAs and inherited IRAs, and SEP or SIMPLE IRAs that are no longer receiving plan contributions.
- An IRA owner can direct up to \$100,000 per year to be paid as a QCD.
- QCDs can only be made to organizations eligible to receive tax-deductible contributions.
- QCDs cannot be made to a donor-advised fund, a private foundation, or similar entities. You cannot receive a benefit, such as attending a function put on by the charity, from the donation.



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## AVOID TAX TRAPS WHEN MOVING ASSETS

Since IRAs became available in 1975, the portability rules have relaxed to allow retirement savers to move their assets among different retirement accounts. When you change jobs or retire, you can preserve your tax-deferred retirement savings by rolling over your savings from one employer plan to another or to an IRA. If you want to change IRA custodians, you can transfer or roll over IRA assets to another IRA. Pay close attention to the fine print though to ensure you don't inadvertently incur any unnecessary taxation.

### TIPS FOR AVOIDING TAX ON ROLLOVERS

#### ④ Request a direct rollover from your former employer's plan.

If you take a distribution payable to yourself, even if you intend to roll it over to another retirement account within 60 days, the plan administrator will withhold 20% and send it to the IRS as a pre-payment of your tax liability on the distribution. You will be taxed on that 20% (including the additional 10% early distribution tax if you're younger than 59½) unless you come up with that amount out of pocket to include with your rollover deposit.

#### ④ Direct transfer IRA assets to another IRA.

Because you can withdraw cash from an IRA tax-free if you put it back in an IRA within 60 days, the tax laws limit how often IRA owners may make IRA-to-IRA rollovers to once every 12 months. Direct transfers between IRAs, however, are not limited.

#### ④ Roll over in-kind distributions from IRAs.

If you take an in-kind distribution of property, stock, or other investment from a self-directed IRA with the intent to roll it over to another IRA, you must roll over that exact same property. You cannot sell the property or stock outside of the IRA and roll over the cash proceeds. If you take an in-kind distribution from an employer plan though, you may choose to roll it over in-kind to an IRA or sell the asset and roll over the cash proceeds to an IRA.

#### ④ Know your options for company stock before taking it out of your retirement plan.

If you hold company stock in an employer's retirement plan, consider taking an in-kind distribution of the stock and putting it in a taxable account rather than an IRA when you stop working for that employer (or are older than 59½). You will have to pay regular income tax on the principal cost of the stock at the time you distribute it from the plan,



but the Net Unrealized Appreciation (NUA) - the difference between the cost basis and the market value of the stock when it leaves the plan - will be taxed at the favorable long-term capital gains rate when you sell it from the taxable account. Investment gains earned on the employer stock while held within the taxable account will be taxed at the short or long-term capital gains rate depending on how it's held. On the other hand, if you roll over employer stock to an IRA, you lose the NUA option and will pay tax at your regular income tax rate in the year you distribute the asset from the IRA.

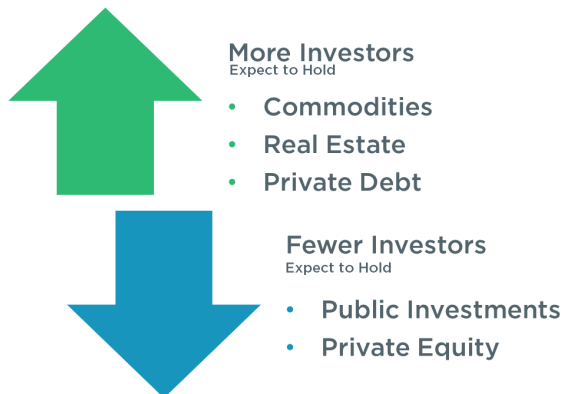
## LOOKING AHEAD

For 2023, inflation, rising interest rates, and national and global events will continue to affect the U.S. economy. It's difficult to predict the impact these factors will have on your income, investments, and everyday finances. What is known is that income tax rates will increase after 2025 if legislation is not passed to extend them. Take a proactive approach to financial planning with tax-smart strategies now to help prepare for future tax rate increases and help reach your retirement and other financial goals.



## EXPLORING INVESTMENTS?

Looking to alternatives to help stabilize market volatility is more popular than ever. In STRATA's 2022 Self-Directed IRA Survey Report, individual investors shared their interest in investment types in the upcoming 12-24 months. We found:



Tax-smart IRA strategies like maxing out IRA tax benefits, diversifying asset location, leveraging Roth conversions, minimizing RMDs, and avoiding taxation when moving retirement assets are just a few ways you can take control of when and how you'll pay tax on your retirement savings. Connect with your legal, financial, and/or tax professional for more information on how you can utilize these strategies.



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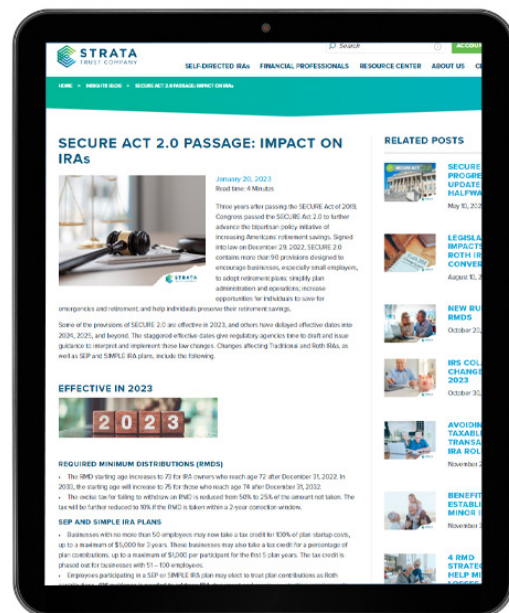


## SECURE ACT 2.0: IMPACT ON IRAs

The tax laws and advantages associated with retirement savings are always changing. It's important to stay informed about what's on the horizon when you're designing a long-term financial strategy. Signed into law on December 29, 2022, SECURE 2.0 contains more than 90 provisions. Below are some of the changes that will impact your IRA.

- The Traditional and Roth IRA age 50+ catch-up limit would be indexed with the cost-of-living adjustments (COLAs) each year.
- The age for beginning required minimum distributions (RMDs) would increase to 75 by 2033.
- The excise tax for missed RMDs would decrease from 50% to 25% of the amount missed, and 10% if the failure is corrected and the excise tax is paid timely.
- The amount eligible to be paid as a tax-free QCD would be indexed each year.
- SEP and SIMPLE IRAs could be designated as Roth IRAs.
- The SIMPLE IRA catch-up contribution limit would increase to \$5,000 for participants ages 62–64.

- SIMPLE IRA plan employers could treat their employees' student loan payments as deferrals for purposes of SIMPLE IRA matching contributions.
- The small business plan start-up tax credit would increase to 75% or 100% of SEP or SIMPLE IRA plan start-up costs, depending on the number of employees.
- Only the amount involved in a prohibited transaction would be taxable, rather than the entire IRA.



*Learn more about SECURE Act 2.0 and what provisions are effective in 2023, 2024, 2025, and beyond.*



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## ABOUT US



# STRATA TRUST COMPANY

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STRATA Trust Company is a premier national custodian for alternative assets and non-exchange traded investments in self-directed IRAs. STRATA has been helping investors use their retirement account funds to invest since 2008.

With offices in Waco and Austin, Texas, our team's vast experience in handling the details and complexities that alternative investment transactions require is unrivaled. Our seasoned team's experience in the custody of alternative assets spans over 350 years. With a well-established reputation for honesty and integrity, STRATA is committed to delivering responsive, flexible, and innovative solutions.

At STRATA, we work to ensure that the highest standards for safety and soundness are met. As a subsidiary of Horizon Bank, SSB, STRATA is a Texas-chartered trust company regulated by the Texas Department of Banking, which has long set the benchmark among state banking regulators. Strict controls are in place to ensure the safety of uninvested cash, and independent auditors are retained to conduct regular audits of our operations.

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