Tax Management Ideas for the New Year

Now could be a great time to reassess tax strategies. Do you have clients approaching retirement who need to start planning their distributions? Are you up to date on 2025 changes that could help enhance their financial strategies? Here are some key considerations to keep in mind.

Changes in tax laws and inflation-adjusted thresholds and the potential sunset of the Tax Cuts and Jobs Act (TCJA) provisions present fresh opportunities to refine tax strategies for clients. Proactive tax management can help clients mitigate liabilities, prioritize savings, and pursue financial goals. We've outlined key strategies to consider for the year ahead.

Managing Required Minimum Distributions (RMDs)

Distribution planning is key for efficient tax strategies, especially for distributions your clients may not need. In these cases, clients may consider:

- **Qualified Longevity Annuity Contracts (QLACs)**. A QLAC can be a valuable tool for reducing RMDs. In 2025, a client can allocate up to $210,000 from his or her IRA or qualified account into a QLAC. For example, a client with $1,000,000 in qualified accounts can lower the year-end balance used to calculate RMDs to $790,000, effectively reducing the RMD amount. Additionally, a QLAC provides a strategy for income later in life, as payments can be deferred until age 85.
- **Qualified Charitable Distributions (QCDs)**. A QCD is one way to lower taxable income for the year. Despite the Setting Every Community Up for Retirement Enhancement (SECURE) Act 2.0 raising the RMD age to 73, individuals can still make QCDs starting at age 70½. In 2025, clients can contribute up to $108,000 through a QCD, reducing their IRA balances and, in turn, reducing future RMD calculations. This strategy may be appropriate for clients who are charitably inclined and have substantial qualified assets.
- **Roth Conversions**. Another strategy that can help reduce future RMDs is converting traditional IRA accounts into Roth IRAs. As a client approaches the age at which RMDs begin, he or she may convert portions of IRA assets into a Roth IRA. This reduces the balance of the traditional IRA, resulting in a lower year-end balance and a smaller RMD calculation. Roth conversions during low tax years can reduce the balance in retirement accounts, minimizing future RMDs that could be taxed at higher rates. Additionally, Roth IRAs offer tax-free income, provided withdrawals meet the requirements for qualified distributions (e.g., a five-year holding period and the client being at least age 59½). This approach also can enhance tax diversification in retirement. Please note that if clients have already reached the age at which they should being taking RMDs, they must take the RMD prior to any conversions.

Prioritize Retirement Savings by Maximizing Contributions

Maximizing contributions to retirement plans by taking full advantage of contribution limits can help build retirement savings, but it also reduces taxable income for the current year. IRA and catch-up contribution limits remain unchanged for 2025. However, contribution limits for employer-sponsored plans have increased. Additionally, starting this year, these plans—along with SIMPLE IRAs—allow enhanced catch-up contributions for clients ages 60 to 63.

Plan Ahead to Address Tax-Management Goals

With the uncertain sunset of the TCJA, 2025 could be shaping up to be a complex year for tax planning. By proactively planning and leveraging tools such as QLACs, QCDs, and Roth conversions, clients can effectively lower RMDs and manage their taxable incomes more smoothly. Additionally, taking full advantage of increased contribution limits and enhanced catch-up provisions can help clients boost retirement savings while benefiting from certain tax treatment.

Remember—one meeting can go a long way. Staying ahead with these strategies can lead to a more tax efficient retirement plan, helping to ensure clients are well-positioned to achieve their financial goals. As always, thoughtful planning and collaboration with clients' tax professionals will be key to navigating these changes and maximizing opportunities in 2025.

ACTIONS YOU CAN TAKE RIGHT NOW

- **Explore tax-management strategies for clients taking RMDs.**
- **Discuss options to help with tax management for large qualified accounts.**
- **Ensure clients are taking advantage of IRA contributions and planning for elective deferrals for the year.**

Additional Resources and Links

2024 Federal Tax Amount Limits

2025 Federal Tax Amount Limits

RMD Changes for Designated Beneficiaries in 2025

For more information about retirement planning, please contact our Retirement Strategies Group at RSG@PacificLife.com or (800) 722-2333, ext. 3939.

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In order for the contract to be eligible as a QLAC, certain requirements under Treasury regulations must be met, including limits on the total amount of purchase payments that can be made to the contract. Qualified contracts, including traditional IRAs, Roth IRAs, and QLACs, are eligible for favorable tax treatment under the Internal Revenue Code (IRC). Certain payout options and features may not comply with various requirements for qualified contracts, which include required minimum distributions. Therefore, certain product features, including the ability to change the annuity payment start date, accelerate payments, and to exercise withdrawal features or payout options, may not be available or may have additional restrictions.

Annuity withdrawals and other distributions of taxable amounts, including death benefit payouts, will be subject to ordinary income tax. For nonqualified contracts, an additional 3.8% federal tax may apply on net investment income. If annuity payments, withdrawals, and other distributions are taken prior to age 59½, an additional 10% federal income tax may apply. A withdrawal charge and a market value adjustment (MVA) also may apply. Withdrawals will reduce the contract value, the value of the death benefit, and also may reduce the value of any optional benefits.

If there is any change to the Internal Revenue Code or Treasury regulations related to RMDs, Pacific Life reserves the right to modify or eliminate the treatment of RMD withdrawals, but only to the extent necessary to comply with the change to the rules.

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