New IRA Restrictions and Mandatory Distributions

When reports surfaced that PayPal founder and billionaire Peter Thiel had invested his Roth IRA in private equity and private stock in his own company and managed to turn an account worth less than $2,000 in 1999 into a $5 billion nest egg free from taxes, it caught the attention of Congress. Thiel will never have to pay the government a penny in taxes on his investment windfall.

Thiel may be the most widely-publicized example of someone who took full advantage of the Roth rules, but he isn't the only one. Hedge fund manager Robert Mercer reportedly has $31.5 million in his Roth IRA, and Warren Buffett, one of the richest men in the world, has $20.2 million socked away in his tax-free retirement account. One of Buffett's Berkshire Hathaway executives has been even more aggressive; he has a Roth valued at $264.4 million, and Alden Global Capital hedge fund manager Randall Smith owns a Roth valued at $252.6 million.

In the tax package that recently passed the House Ways & Means Committee, it was pointedly noted that Thiel and others were able to basically put their own companies into the Roth, creating a tax-free corporation that was never envisioned under U.S. tax law.

That will no longer be possible if the House bill becomes law. It specifies that, going forward, IRAs and Roth's will only be allowed to invest in publicly-traded securities, and it specifically prohibits these accounts from owning private equity, hedge funds and other investments that are only available to certain wealthy insiders. Current owners would be required to sell these exotic holdings within two years, and use the proceeds to buy a public, SEC-registered investment. (If they comply within this time periods, there will be no tax penalties.)

The bill would go a long step further and require people who are lucky enough to have more than $10 million in a traditional or Roth IRA from making any further contributions and impose new required minimum distributions on those accounts. Anyone with more than $400,000 in taxable income and over $10 million in a traditional or Roth IRA at year's end would have to withdraw at least half of the excess the following year. The goal appears to be to create a cap of $10 million on all retirement accounts that escape annual taxation going forward and eliminate the tax-free corporation from the U.S. economic landscape.

Sources:

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Jeffrey Broadhurst
MBA, CFA, CFP
Broadhurst Financial Advisors, Inc.

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Our emailing address:
1911 W Point Pike, POB 301
PA 19486, United States

Contact us:
Phone: (215) 325-1595
Email: jeff@broadhurstfinancial.com