Turning 70 1/2 This Year?

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Article Highlights:

- Turning 70 1/2
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If you are turning 70 1/2 this year, you may face a number of special tax issues. Not addressing these issues properly could result in significant penalties and filing hassles.

- **Traditional IRA Contributions** – You cannot make a traditional IRA contribution in the year you reach the age of 70 1/2 Contributions made in the year you turn 70 1/2 (and from then on) are treated as excess contributions and are subject to a nondeductible 6% excise tax penalty for every year in which the excess contribution remains in the account. The penalty, which cannot exceed the value of the IRA account, is calculated on the excess contributed and on any interest it may have earned.

  You can avoid the penalty by removing the excess and the interest earned on the excess from the IRA prior to April 15 of the subsequent year and including the interest earned on the excess in your taxable income.

  Even though you can no longer make contributions to a traditional IRA in the year you reach age 70 1/2 you can continue to make contributions to a Roth IRA, not to exceed the annual IRA contribution limits, provided you still have earned income, such as wages or self-employment income, at least equal to the amount of the contribution.

  If you are married to a non-working or low-earning spouse who has not yet reached age 70 1/2 and you have earned income, your earnings can still be used to qualify your spouse for a contribution to a spousal IRA, even if you are 70 1/2 or older and can't contribute to your traditional IRA.

- **Required Minimum Distributions (RMDs)** – You must begin taking required minimum distributions from your qualified retirement plans and IRA accounts in the year you turn 70 1/2 The distribution for the year in which you turned 70 1/2 can be delayed to the subsequent year without penalty if the distribution is made by April 1 of the subsequent year. That means two distributions must be made in the subsequent year: the delayed distribution and the distribution for that year. In the following years, your annual RMD must be taken by December 31 of each year.

- **Still Working Exception** – If you participate in a qualified employer plan, generally you need to start taking required minimum distributions (RMDs) by April 1 of the year following the year you turn 70 1/2. This is your required beginning date (RBD) for retirement distributions. However, if your plan includes the "still working exception," your RBD is postponed to April 1 of the year following the year you retire.

  Example: You reached age 70 1/2 in 2015, but chose to continue working and did not retire until June of 2017. Provided your employer's plan includes the option, you can make the "still working election" and delay your RBD until no later than April 1, 2018.

Caution: This exception does not apply to an employee who owns more than 5% of the company. There is no “still working exception” for IRAs, Simple IRAs, or SEP IRAs.

- **Excess Accumulation Penalty** – When you fail to take an RMD, you are subject to a draconian penalty called the excess accumulation penalty. This penalty is a 50% excise tax of the amount (RMD) that should have been distributed for the year.

  Example: Your RMD for the year is $35,000, but you only take $10,000. Your excess accumulation penalty for failing to take the full amount of the distribution for the year would be $12,500 (50% of $25,000).

  The IRS will generally waive the penalty for non-willful failures to take your RMD, provided you have a valid excuse and the under-distribution is corrected.

As you can see, turning 70 1/2 can complicate your financial situation. If you need assistance with any of the issues discussed here please give my office a call (972) 731-2539.