ED SLOTT'S IRA ADVISOR

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Tax & Estate Planning For Your Retirement Savings

WHAT'S INSIDE?

Happy Holidays

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October Deadline Missed – *Now What?*

October 15 is an important date as it is the final cutoff for several IRA transactions. Typically, clients are instructed on how to correct errors prior to this deadline. However, now that October 15, 2019 is in the rearview mirror, the procedure for fixing certain 2018 mistakes has changed and some opportunities might be lost. *Time to deal with the consequences.*

Excess IRA Contributions

The cutoff for removing an excess IRA contribution for 2018 without penalty was October 15, 2019. *Maybe a client was age 70½ or older in 2018 and made an ineligible contribution to a traditional IRA? Maybe a client's income ended up being higher than expected, ultimately making him ineligible for a Roth IRA contribution?*

Regardless of the reason, if there is an excess contribution, it can be corrected by withdrawal, and only the excess contribution amount needs to be withdrawn.

The good news is that in an odd tax code anomaly, since we are after the October 15 deadline, any net income attributable (NIA) to the excess contribution can remain in the traditional or Roth IRA.

The bad news is that there will be a 6% excess contribution penalty, and IRS Form 5329 will need to be filed to pay it. Excess contribution mistakes do not go away on their own. The 6% penalty will apply each year the excess contribution remains in the IRA.

Example: Jake is a clumsy sales representative who usually makes very little money. Even so, like clockwork, he contributes the maximum dollar amount allowed ($5,500 for 2018) to a Roth IRA every January and sets his New Year resolution for a more lucrative year.

Well, even a blind squirrel will occasionally find a nut. In 2018, Jake stumbled into an unexpectedly successful sales year and earned a sizable commission check that December. His modified adjusted gross income (MAGI) for the year was $250,000, well above the 2018 Roth IRA phase-out range for a single tax filer ($120,000 - $135,000).

Unfortunately, Jake failed to realize he was over the Roth income limits. His $5,500 Roth IRA contribution is now worth $6,500. Since the mistake was identified after October 15, 2019, Jake must remove the excess contribution of $5,500. The $1,000 of NIA can remain in the Roth IRA. Jake must also file Form 5329 and pay a $330 penalty ($5,500 x 6%).

Besides withdrawal, another option to correct excess IRA contributions exists. Jake could have elected to carry forward the excess and apply the overage to future years.