TD Ameritrade

The TICKER TAPE®
Pearls and Insights for Investors

Boomer RMD Requirements: Mistakes to Avoid, Q&A

By Kira Brecht | MARCH 22, 2017

After decades of socking away money in retirement funds, baby boomers who turn 70 1/2 this year hit the required minimum distribution (RMD) age threshold. The government The government requires that you start drawing down your retirement assets via RMD, or else face a stiff penalty—50% of the RMD.

Avoid These Common Mistakes

This isn’t a complicated transaction, but there are details that need to be managed in order to avoid big penalties. "There will be about 10,000 boomers a day turning 70 1/2 for the next 18 or so years, and that’s a lot of RMDs that will be coming out, whether they want them or not," says Thomas J. O’Connell, president of International Financial Advisory Group, Inc.

"The most common mistake I see are people not taking them or not taking the correct amount. There is still, to this day, a large swath of people who have no idea that they are supposed to take RMDs," O'Connell says. Additionally, he says some people have no idea they are required to pay taxes on the distribution, and are stunned when they get a tax bill.

Another common mistake relating to retirement accounts is having no beneficiaries designated to your accounts, or having the wrong beneficiary named. "This is the biggest mistake I come across with IRAs and 401(k) accounts," O'Connell says.

Turning 70 1/2? Six Things You Need to Know

1. How much do you need to withdraw? RMDs will vary from person to person, account to account, and are based on your age and the value of your account on December 31 of the previous year. Worksheets and tables are available on the IRS website.

Here's an example. "If I turned 70 1/2 and had to take a RMD this year and my account value was $100,000 on December 31, 2016, my RMD amount would be $3,623. As I get older, the percentage of my account that I need to take out gets larger," O'Connell says.

2. Are there exceptions? Of course. A Roth IRA has no RMDs during the lifetime of the owner. However, Roth IRAs are subject to RMDs after the death of the owner, and the same 50% penalty will apply.

3. How will it affect your taxes? "RMDs count as ordinary income in the year you receive the distribution. It will be added in to all your other income for that year and be taxed according to your tax bracket," O'Connell says.

4. Will this impact my Social Security check? It definitely could, and probably will, O'Connell warns. "RMDs count when calculating your total income, and if you are over the Social Security thresholds, either 50% or 85% of your social security benefits will be taxable," he explains.

5. What is the deadline to take the RMD? Your first distribution is due the year you turn 70 1/2, but you can postpone it to no later than April 1 of the following year. After that first year, the annual deadline is December 31. "Bear in mind that if you postpone that first distribution into the next year, you'll have to take two distributions in one tax year," O'Connell says.

6. What is the penalty? It's a big one, which is why it is important to make sure you adhere to the guidelines. "It's one of the worst, if not the worst penalty in the tax code. If you fail to take a distribution, the penalty is 50% of what you were supposed to take. So if my RMD last year was $10,000 and I didn't take it, my penalty is

$5,000. If I didn’t take everything I was supposed to, say I only took $5,000 of the $10,000, then my penalty is 50% of what I missed or $2,500," O'Connell says.

Consider a Roth Conversion

Another thing to consider is converting some of your IRAs to Roth IRAs either prior to or after age 70 1/2. "It’ll be a taxable event when it occurs, but it could save you taxes in the future," O'Connell says.

Unlike a traditional IRA, which is tax-deferred until withdrawn, a Roth IRA is taxed up front, but is tax-free when you take it as a distribution. And, again, with a Roth there is no RMD during the lifetime of the owner. But a word of caution: if you taking an RMD this year and are considering converting your traditional IRA to a Roth IRA this year, you must first satisfy this year's RMD. In other words, you're not allowed to convert RMD money.

"One important piece of information I can give about RMDs is this: don’t do it yourself. Find an advisor who has very specific training in this area, because it is far more complicated than most people realize," O'Connell concludes.