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## The Post-70 ½ Retirement Plan Contribution Rules

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By **William H. Byrnes, Robert Bloink** | August 22, 2016

By the time many clients reach age 70 ½, they are ready to enjoy retirement and are well aware of the obligation to begin taking required minimum distributions (RMDs) from various retirement accounts.

Although this may generally be the case, there are a variety of reasons why a client may wish to continue contributing to retirement accounts past the age when RMDs begin — perhaps the client is still working and trying either to reduce taxable income or make up for missed contributions during earlier working years.

Whatever the reason, clients must understand that they cannot *always* continue contributing to their accounts after they reach age 70 ½. Different rules govern each type of account, so the client must carefully examine his or her portfolio of retirement accounts to determine where a post-70 ½ contribution may be permissible — as well as the RMD impact of the contribution.

## The IRA Post-70 ½ Contribution Rules

The rules for post-70 ½ IRA contributions depend upon whether the account is a traditional IRA, Roth IRA or SEP IRA. Direct contributions to a traditional IRA are not permitted after the client reaches age 70 ½, although the client may roll funds from another type of retirement account into his or her traditional IRA.

Conversely, the client may contribute directly to a Roth IRA after he or she has reached age 70 ½ (up to the annual \$6,500 limit, which includes a \$1,000 catch up amount). Direct Roth IRA contributions, however, are subject to income limitations that apply to reduce the contribution limits for taxpayers who earn more than \$184,000 (married taxpayers) or \$117,000 (single taxpayers) in 2016.

Further, the client must have annual compensation that is at least equal to the direct contribution (meaning that the taxpayer must still be working in some capacity to contribute directly, as the compensation must be earned income, rather than investment income or Social Security benefits).

Rollovers to Roth IRAs are permitted, but clients must remember that a traditional IRA RMD cannot be characterized as a rollover transaction. Therefore, if the client wishes to contribute his or her RMD to a Roth account, the client is limited to depositing \$6,500 (or 100% of compensation) of the RMD into the Roth for the year, assuming that the income thresholds are not exceeded.

SEP IRA contributions are also permitted after the client reaches age 70 ½. These contributions are limited to 25% of the client's compensation, or \$53,000 (in 2016), whichever is less. RMD rules do apply once the taxpayer reaches 70 ½, so the client may be both making contributions and taking RMDs from the account.

## Annuities As an RMD Answer

While many advisors have counseled against purchasing an annuity with IRA funds in the past, in today's post-recession world, there are several reasons why a client may be interested in the annuity-within-an-IRA strategy. However, as with any retirement income planning strategy, the pitfalls associated with a poorly executed annuity purchase strategy can cause unnecessary expenses and disappointment down the road.

This is especially true if the client is planning to use the annuity to simplify his or her IRA RMD obligations. Because a separate set of rules governs each individual type of annuity that may be held within an IRA for RMD purposes, it is important that the advisor carefully examine the proposed annuity in light of the client's goals.

In general, a client may hold either an immediate or deferred annuity within his or her IRA. An immediate annuity allows the client to begin receiving annuity payments immediately (or very shortly after the contract is purchased). Once annuitized, the value of these types of annuities are excluded from the value of the IRA for purposes of calculating the RMDs for the non-annuity IRA assets.

Importantly, the client should be advised that he or she will be required to calculate RMDs on those non-annuity assets held within the IRA even though he or she is receiving annuity payments. It is also important to note that immediate annuities purchased within an IRA must provide that payments will begin no later than when the client reaches 70 ½, and the minimum guarantee term generally must end around the time the client reaches age 96.

On the other hand, the fair market value of a non-annuitized deferred annuity that is held within an IRA is included in the value of the account (as of the end of the prior year) in computing RMDs for the year.

## **Employer-Sponsored 401(k) Accounts**

Clients who are still working after age 70 ½ may generally continue contributing to employer-sponsored 401(k) accounts and SEP IRAs. In fact, employers must continue to make employer contributions to the SEP IRA of an employee who is over age 70 ½ if it makes similar contributions to younger employees' accounts.

If the client plans to work past age 70 ½, he or she can avoid RMDs by leaving the funds in the employer-sponsored 401(k). As long as the client continues to work for the same employer that sponsors that plan, and does not own 5% or more of the company, he or she can avoid taking distributions from a 401(k), thereby avoiding the associated income tax liability that those distributions generate.

Continuing to make retirement account contributions past age 70 ½ is an individual decision that may make sense in a variety of scenarios. However, whether a client is permitted to make those contributions is governed by strict IRS rules that vary for each type of retirement account.