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FOR IMMEDIATE RELEASE
Monday, March 2, 2015

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Tax Solutions for Baby Boomers

The Baby Boom generation, the children born in the post-World War II years between 1946 and 1964, includes about 76 million people. Now that generation is heading into retirement, with roughly 10,000 Boomers expected to retire every day between now and 2030. If you or a family member are part of this group, do you know what tax and other financial issues you should be considering? The Tennessee Society of CPAs provides some timely tips.

Be Aware of the RMD Deadline

Required minimum distributions (RMDs) can create a potentially expensive pitfall for those who aren't aware of the important rules surrounding them. The RMD rules apply to traditional individual retirement accounts (IRAs) and IRA-based plans such as SEPs, SARSEPs and SIMPLE IRAs. If you have an IRA, you must take your first required minimum distribution for the year in which you turn age 70 ½. However, the first payment can be delayed until April 1 of the year following the year in which you turn 70 ½. So, if you turned 70 on, say, May 15, 2014, you hit 70 ½ six months later, on November 15, 2014, you would need to start taking IRA distributions by April 1, 2015. For all subsequent years, including the year in which you were paid the first RMD by April 1, you must take the RMD by Dec. 31 of the year. The amount of the RMD is generally calculated by dividing the prior Dec. 31 balance of your account by a life expectancy factor, published in Internal Revenue Service tables. Any withdrawals you take will be included in your taxable income (unless they have already been taxed, as would be the case with a Roth IRA, for example). If you miss the RMD deadline, fail to withdraw a RMD or fail to withdraw the full amount of the RMD, the amount not withdrawn is taxed at 50 percent. It’s important to note that the RMD rules do not apply to Roth IRAs while the owner is alive.

Don’t Confuse IRAs and 401(k)s

The RMD rules apply to all employer-sponsored retirement plans as well, including profit-sharing plans, 401(k) plans, 403(b) plans and 457(b) plans. While RMDs are required beginning at age 70 ½ for IRAs, with an employer-sponsored retirement plan, distributions begin at 70 ½ years of age or, if later, the year in which you retire, as long as your employer’s plan allows it. You should also be able to continue to contribute to the plan as long as you work, unless you own 5 percent or more of the business. If you are a 5 percent owner of the business sponsoring the retirement plan, the RMDs must begin once you are 70 ½. It’s very important, then, to understand the different rules for each type of retirement account. You could face a penalty if you don’t take RMDs as required, but you could miss out on some tax benefits if you take them before it is necessary. Sound a little confusing? It can be. That’s why it’s a good idea to consult your CPA about how the RMD rules affect your specific situation.

Taxes on Social Security Income

Want to minimize taxes on Social Security income? Your tax rate on Social Security varies depending on your total taxable income, including distributions from retirement accounts. There are a number of steps you can consider to reduce that rate. For example, you could take distribution from a Roth IRA rather than from a traditional IRA, since a qualified Roth IRA withdrawal should generally not be taxable. Keep in mind, too, that you can delay collecting Social Security. If you do, the amount you receive will increase until you reach age 70. If you plan to work into your 60s or 70s, you might consider putting off taking Social Security benefits, even if you've reached full retirement age, until you've stopped working. The result: You'll get higher benefits and the tax you pay on them may be reduced.

Your CPA Can Help

As the Boomers approach retirement, it's clear that advance planning and smart decision making can help them reduce their tax concerns and ensure sufficient retirement income. Your local CPA can help you address the many tax and related issues involved in retirement. Be sure to turn to him or her for sound financial advice.

About Money Management

Money Management is a column on personal finance that is a joint effort of the AICPA and the Tennessee Society of CPAs, as part of the profession's nationwide 360 Degrees of Financial Literacy program. Members of TSCPA are CPAs residing and practicing primarily in Tennessee in all areas of public accounting, education, government, business and industry. TSCPA offers a speakers bureau for many types of business and educational engagements. For details, visit www.tscpa.com. TSCPA is headquartered in Brentwood, Tenn.