

Resolving IRA Excesses

Excess Contribution Correction

Before TRDD+
▼
Remove or recharacterize with the net income attributable.

After TRDD+
▼
Redesignate or remove excess amount.

Unwanted Contribution Correction

Before TRDD+
▼
Remove or recharacterize with the net income attributable.

After TRDD+
▼
Cannot remove. Leave in IRA as annual contribution.

+ If IRA owners file their taxes by their regular or extended deadline, they are granted an automatic six month extension for removal of excess to October 15.

Recharacterize – A recharacterization is a reportable transfer of all or part of a contribution, plus earnings/loss, from a Traditional IRA to a Roth IRA, or from a Roth IRA to a Traditional IRA. An individual may be able to correct an excess using recharacterization if the excess is due to the individual's being ineligible for the specific type of IRA to which he or she contributed, but he or she is eligible for the other type IRA. A recharacterization may also be used to undo a conversion.

Net income/loss attributable – Net income/loss attributable is the amount of earnings specific to an excess contribution amount being removed, or a contribution (or conversion) being recharacterized.

Redesignate – To redesignate means to apply an excess contribution to a later tax year. The individual is still responsible for paying the six percent penalty, but leaves the contribution and earnings/loss in the IRA.

Remove Before the Deadline

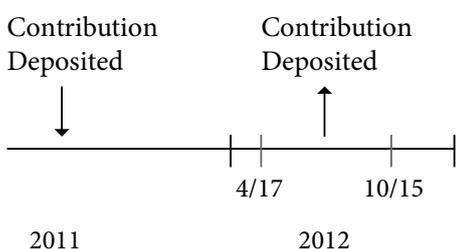
The IRA Owner

1. IRA owner avoids 6% IRS penalty
2. Contribution is not claimed as deductible or basis
3. NIA taxable for year in which contribution was made
4. 10% penalty on NIA, unless exception applies

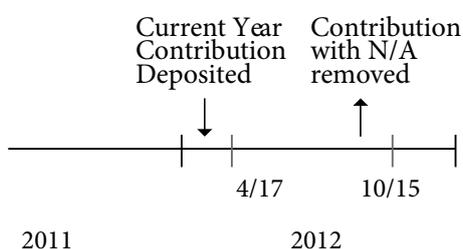
The Financial Organization

1. Remove excess contribution with NIA
2. Original contribution reported on Form 5498
3. Form 1099-R reporting required
Code P – Contribute in year, remove subsequent year.
Code 8 – Contribute and remove same year.

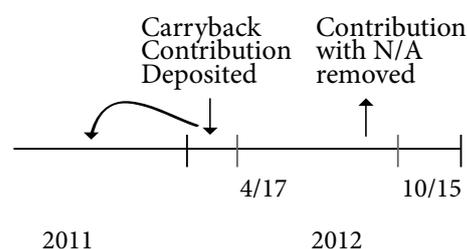
Code P



Code 8



Code 8



Recharacterize

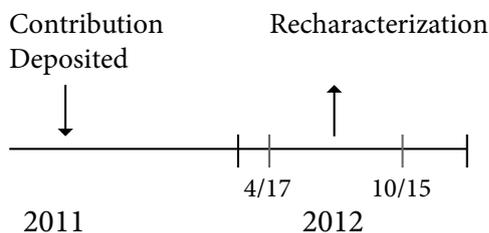
The IRA Owner

1. The IRA owner irrevocably elects to treat the contribution as having been made to the second IRA rather than the first
2. The IRA owner attaches a statement when he or she files his or her taxes confirming the recharacterization

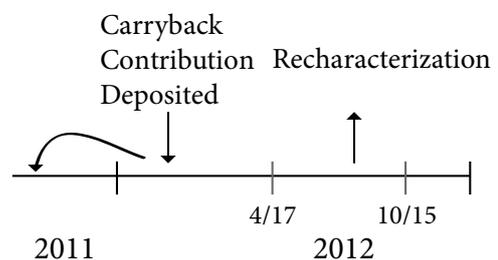
The Financial Organization

1. The financial organization directly transfers the contribution (or conversion) amount, plus any net income/loss attributable, from the first IRA to the second IRA
2. The financial organization reports the distribution from the first IRA.
Code R – Contribute for year, recharacterize subsequent year.
Code N – Contribute for and recharacterize in same year.
3. The financial organization reports the contribution into the second IRA.

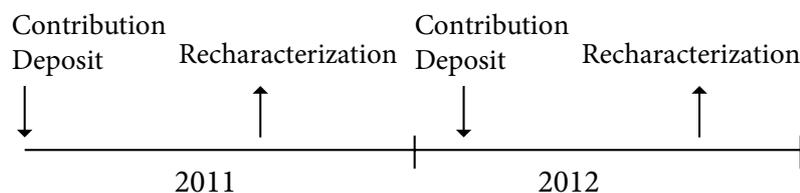
Code R



Code R



Code N



Redesignate

The IRA Owner

1. IRA owner pays 6% IRS penalty – Form 5329
2. IRA owner redesignates for subsequent year – Form 1040 or 8606

The Financial Organization

1. Leave the excess contribution in the IRA
2. Original contribution reported on Form 5498
3. No additional reporting

Remove an Excess – After the Deadline

The IRA Owner

1. IRA owner pays 6% IRS penalty – Form 5329
2. Taxable if total IRA contribution exceeds individual limit (Traditional IRA only)
3. 10% penalty unless exception applies (Traditional IRA only)

The Financial Organization

1. Remove excess contribution
2. Original contribution reported on Form 5498
3. Form 1099-R reporting required



Earnings Calculation Worksheet

| | | | |
|---|---|----|--|
| 1 | Contribution amount to be withdrawn as excess contribution or recharacterized | 1 | |
| 2 | A Fair market value of the IRA on the date the excess contribution is withdrawn or the contribution is recharacterized (prior to the transaction) | 2A | |
| | B Total of all distribution taken from the IRA since immediately prior to the excess/recharacterized contribution originally being made Note: Distributions include, but are not limited to: transfers, rollovers and recharacterizations. Do not include the distribution of the excess/recharacterized contribution. | 2B | |
| | C Amount of investment penalties that will be assessed on the withdrawal of the excess/recharacterized contribution | 2C | |
| | D TOTAL 2 = 2A plus 2B minus 2C | 2D | |
| 3 | A Fair market value of the IRA immediately prior to the excess/recharacterized contribution being made | 3A | |
| | B Total of all distribution taken from the IRA since immediately prior to the excess/recharacterized contribution originally being made Note: Contributions include, but are not limited to the excess/recharacterized contribution, transfers, rollovers, conversions and recharacterizations. | 3B | |
| | C TOTAL 3 = 3A plus 3B | 3C | |
| 4 | Subtract 3C from 2D | 4 | |
| 5 | Divide line 4 by 3C | 5 | |
| 6 | Multiply line 5 by line 1 This is the net income attributable to the contribution. Note: A negative amount represents a loss. | 6 | |
| 7 | Add line 7 to line 1 This is the total amount to be withdrawn to correct the excess contribution or moved as part of the recharacterization. | 7 | |

Note: Earnings must be calculated based on all investments held in the IRA.

