How to Deal with
Excess IRA Contributions

Making excess IRA contributions, also called ineligible contributions, is a common mistake often attributed to confusion about contribution allowances. Contribution allowances are the same for traditional **IRAs** and **Roth IRAs** and the penalties for excesses are the same as well.

Common Reasons for Excess IRA Contributions

Reasons for making an excess IRA contribution include:

- Making more money than expected so your income eligibility range exceeds the IRA contribution limits
- Contributing the max amount to your IRA earlier in the year, then forgetting and contributing again
- Contributing more than your earned income for the year (your contribution cannot be more than what you’ve earned)
- Investing automatically at too high a level and exceeding your contribution limits
- Thinking you can contribute the max combined amount to multiple IRAs individually rather than a max amount to all combined

IRA Income and Contribution Limits

For the 2023 tax year, the max amount you can make to a traditional or Roth IRA, individually or combined, is:

- $6,500 if you’re under 50 years old
- $7,500 if you're 50 or older

This means if you’re 49 years old, for example, and wish to contribute to a Roth as well as a traditional IRA, you can contribute $2,500 to one and $4,000 to another or a similar combination, but you can’t contribute $6,500 to each.

Similarly, suppose you are over age 50 and wish to contribute the maximum annual amount (which includes the Age 50 Catch-Up) to a Roth and a traditional IRA. In that case, the maximum you can contribute combined is $7,500. For example, $3,000 to your Roth and the remaining $4,500 to your traditional IRA.

Your Roth contributions may be limited based on your Modified Adjusted Gross Income. To determine Roth income contribution limits, see Publication 590-A, Contributions to Individual Retirement Accounts (IRAs) , or consult your tax advisor.

How to Make an Excess Contribution Removal

Once you realize you've made an excess IRA contribution, contacting your plan administrator immediately is essential. They can help you file the appropriate paperwork and remove the excess contribution. Removing the excess contribution **involves withdrawing the ineligible contribution and any earnings from your IRA.**

Traditional and Roth Excess Contribution Removal Deadline

The removal deadline for excess contributions to a traditional IRA or a Roth IRA is your tax-filing deadline. This is typically April 15 of the following year (or October 15 if you're filing an extension).

What is the Penalty for Excess Contributions to an IRA?

The penalty for an excess IRA contribution is 6% on the excess amount for every year the excess stays in your account. Filing an amended return before the October extension deadline can help you avoid the 6% penalty.

Note: If you have contributed to both a traditional and Roth IRA and exceeded the combined limit for both, the IRS requires you to remove the excess from your Roth IRA first.

Other Taxes and Penalties on IRA Excess Contribution Removal

Depending on your age and what type of IRA you have, your earnings on the excess contribution will be taxed as ordinary income. If you're under the age of 59½, you may owe a 10% tax for early withdrawal.

Reminder: You must report any earnings on excess contributions on your income taxes.

If you have exceeded contributions to a Roth IRA, you may be able to fix the excess without penalty.

How to Report an Excess Roth IRA Contribution

The IRS allows you to withdraw the excess contribution from a Roth IRA without penalty if you meet the distribution requirements:

- You must be 59½ years old.
- You must have held the Roth IRA for a period of five years.

Reporting an excess Roth IRA contribution generally involves the same process as reporting an excess contribution to a traditional IRA. As soon as you notice the excess contribution, you should contact your plan administrator. If you have already filed your tax return, file an amended tax return.

Ways to Fix Excess Roth IRA Contributions

Recharacterization

With an excess contribution to either a traditional or Roth IRA, you could also **recharacterize the excess contribution.** This means you can transfer the excess amount and earnings from one type of IRA to another if you haven't already maxed out your total IRA contributions. This is a reportable transaction to the IRS, but it is nontaxable.

Apply the Excess Contribution to the Next Year

If you're not able to file an amended return in time, you can carry the excess contribution over into the new tax year. You'll still pay a 6% penalty for the year in which the excess contribution was made, but you won't have to pay a future penalty.

Let's say you're 60 years old, so your IRA contribution limit is $7,500 for the year. You've made an excess contribution of $1,000 for a total of $8,500. You can apply the $1,000 excess contribution to next year's IRA, which means you'll only be able to contribute $6,000 next year. You'll pay the 6% penalty or $60 on the $1,000 excess contribution this year, but next year you won't pay any penalty (unless, of course, you make excess contributions again).

Withdraw the Excess Contribution the Following Year

If you're unable to withdraw the excess contribution before you file taxes or make an amended tax return, you can still withdraw the excess contribution after tax filing. You'll pay the 6% penalty tax for every year the excess amount remains in your account.

Note that there are certain conditions for fixing excess Roth IRA contributions:

- If you need to remove an excess contribution from a Roth IRA, you must remove it from the Roth which received the excess. You can't pull from a separate Roth account.
- If you made a Roth IRA contribution earlier in the year and later in the year and the latter contribution is the one considered the "excess contribution." You can't remove the earlier contribution, even if it would help even things out.

How to Calculate Earnings on Excess Roth IRA Contributions

Earnings on excess Roth IRA contributions are known as net income attributable or NIA. The formula for NIA is:

Excess Contribution x [(Adjusted Closing Balance – Adjusted Opening Balance) ÷ Adjusted Opening Balance = Net Income Attributable

To ensure an accurate estimation of earnings on excess contributions, consult with your tax advisor.

Adapted from Mission Square Retirement

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