The Hidden Traps of RMDs—and How Retirees Can Outsmart Them

Introduction

Required Minimum Distributions (RMDs) mark a turning point in retirement: the moment when the IRS begins collecting taxes on decades of deferred savings. Starting at age 73, retirees must withdraw the required minimum distribution from traditional IRAs, 401(k)s, and similar accounts. While the rules sound simple, the ripple effects can be costly—higher taxes, Medicare surcharges, or missed opportunities for charitable giving.

Even seasoned retirees stumble into the same traps. Here's how to avoid them.

1. Waiting Until the Deadline to Plan

RMDs are not a one-year problem; they require a lifetime tax strategy.

Many retirees only think about RMDs when they receive the first withdrawal notice. By then, options are limited.

- **Why it matters:** RMDs can push retirees into higher tax brackets, especially when combined with Social Security, IRMAA, and pension income.
- **Smart move:** Begin planning in your 60s. Consider partial Roth conversions during years when income is lower. For example, delaying Social Security until 70 creates a tax-efficient window for conversions.

2. Missing the Charitable Shortcut

Charitable retirees often withdraw RMDs, pay taxes, and then donate the remainder. That's an expensive detour.

- **Why it matters:** Withdrawals increase taxable income, which can trigger higher Medicare premiums and Social Security taxation.
- **Smart move:** Use a **Qualified Charitable Distribution (QCD)**. Sending funds directly from an IRA to a charity satisfies the RMD while keeping taxable income lower. For someone donating $10,000 annually, this can save thousands in taxes.

3. Assuming Withholding Is "Set It and Forget It"

The IRS default withholding rate is 10%. For many retirees, that's not enough.

- **Why it matters:** Underpayment penalties and surprise tax bills can derail financial plans.

- **Smart move:** Review tax projections annually. A retiree in a high-tax state may need 20–25% withheld to avoid penalties. Adjusting withholding is simple but often overlooked.

4. Ignoring the Domino Effect of RMDs

RMDs don't exist in isolation. They interact with nearly every part of a retiree's financial life.

- **Social Security:** Higher income can make up to 85% of benefits taxable.
- **Medicare:** Crossing income thresholds can trigger IRMAA surcharges, raising premiums by hundreds per month.
- **Deductions:** Larger RMDs can reduce eligibility for certain tax credits in OBBA 3.

Smart move: Model the impact before taking withdrawals. Financial planners should run "tax maps" showing how RMDs affect overall income.

5. Treating Minimum" as "Maximum.

The word "minimum" misleads many retirees into thinking they should only withdraw the required amount.

- **Why it matters:** Limiting withdrawals to the minimum can lead to ballooning account balances, which in turn create larger RMDs later.
- **Smart move:** Consider taking more than the minimum when it makes sense. Extra withdrawals in a low-tax year or Roth conversions can reduce future RMDs and offer greater flexibility for heirs. Provide more flexibility for heirs.

Retiree's RMD Checklist

Before Age 73 (Preparation Phase):

- Review projected tax brackets.
- Use Roth conversions during lower-income years.
- Delay Social Security if possible.
- Explore Qualified Charitable Distributions (QCDs) starting at age 70½.

At Age 73 (First RMD Year):

- Calculate your RMD using IRS tables.
- Adjust withholding—don't rely on the default 10%.

- Coordinate RMDs with Social Security and pensions.
- Send funds directly to the charity if donating.

Ongoing (Annual Review):

- Reassess tax bracket and Medicare thresholds.
- Adjust withholding to avoid penalties.
- Consider taking more than the minimum.
- Update estate and beneficiary plans.

Conclusion

- **RMDs are not just a rule; they're a strategic point. Retirees who plan can avoid penalties, reduce taxes, and even enhance their charitable giving. The lesson is clear: don’t wait until age 73 to think about RMDs. Start early, stay proactive, and treat RMDs as part of a broader retirement tax plan.**