SAVING & INVESTING

SO YOU'VE INHERITED AN IRA



NOW WHAT?

Tax-advantaged savings options, such as IRAs, represent a "cost" to the federal government (in the form of delayed/foregone tax revenues). Because of this, the laws governing IRAs are designed to promote the use of IRA savings during the IRA owner's lifetime, and to minimize the ability for taxpayers to use IRAs as a vehicle for long-term, multi-generational wealth transfer.

Fortunately, however, there are still options available to tax-savvy beneficiaries looking to maximize the tax benefits of their IRA inheritance.

KNOW YOUR OPTIONS—MAXIMIZE THE BENEFITS OF YOUR INHERITANCE

While it's impossible to cover all the details associated with beneficiary IRA withdrawal options in a few short paragraphs, the key message is that it's almost always best to "look before you leap." By first identifying the options available to you as an IRA beneficiary, you're much more likely to make a well-informed decision that meets your personal objectives while also maximizing the available tax-shelter benefits of your IRA inheritance.

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OPTIONS FOR SPOUSE BENEFICIARIES

As the spouse beneficiary of a deceased IRA owner, you have considerable flexibility. While your options will vary depending on the type of IRA, the age of your spouse at the time of death, and the presence (or not) of other named beneficiaries, your options as a spouse beneficiary fall into two broad categories—you can choose to either treat the IRA as your own or take beneficiary withdrawals from the Inherited IRA.

OPTION #1: TREAT THE IRA AS YOUR OWN

As a spouse beneficiary, you have a unique option available to you that is not available to other IRA beneficiaries. Spouse beneficiaries are eligible to move funds from an Inherited IRA into an IRA established in their own name. If you have an existing IRA of the same type as the Inherited IRA, you can generally request to have the Inherited IRA funds transferred or rolled over into your existing IRA. On the other hand, if you do not currently have your own IRA, you can establish an IRA in your own name and request that the Inherited IRA funds be transferred or rolled over into your new IRA.

OPTION #2: TAKE BENEFICIARY WITHDRAWALS FROM THE INHERITED IRA

Another option for you as a spouse beneficiary is to maintain your status as a beneficiary and take beneficiary distributions from the Inherited IRA. This option may be potentially advantageous if you are under age 59½ and wish to withdraw funds prior to reaching age 59½ since beneficiary distributions from an Inherited IRA are exempt from the IRS 10% early distribution penalty.

OPTIONS FOR NONSPOUSE BENEFICIARIES

While spouse beneficiaries generally have the option to move inherited IRA funds to their own IRA, this option is not available to nonspouse beneficiaries. Nonetheless, as a nonspouse beneficiary, you typically have the ability to extend the tax shelter benefits of an Inherited IRA. By avoiding an immediate lump sum distribution and minimizing your distributions, you have the potential to significantly increase the value of your tax-sheltered IRA inheritance. How to extend the tax shelter benefits will vary depending on the circumstances (e.g., the type of IRA and the age of the IRA owner at the time of death) and depending on whether you qualify as an "Eligible Designated Beneficiary."

SCENARIO #1: YOU QUALIFY AS AN ELIGIBLE DESIGNATED BENEFICIARY

As a nonspouse beneficiary, to qualify as an "Eligible Designated Beneficiary" you must be

- a minor child (under age 21) of the deceased IRA owner,
- disabled,
- chronically ill, or
- older than—or no more than 10 years younger than—the deceased IRA owner.

If you qualify as an Eligible Designated Beneficiary,[1] you will generally have the option of drawing down the Inherited IRA funds gradually over your life expectancy via annual (or more frequent) withdrawals. Under some circumstances, you may also have the option of electing the 10-Year Rule option. Under this option, you may withdraw funds at any time provided the Inherited IRA is completely depleted by December 31 of 10th year following the IRA owner's year of death.

SCENARIO #2: YOU DO NOT QUALIFY AS AN ELIGIBLE DESIGNATED BENEFICIARY

A nonspouse beneficiary who does not meet the criteria necessary to qualify as an Eligible Designated Beneficiary must generally deplete an Inherited IRA by no later than December 31 of the 10th year following the IRA owner's year of death. In situations where a Traditional IRA owner passes away on or after their required beginning date, such nonspouse beneficiaries are also required to take annual minimum distributions in addition to the requirement that the Inherited IRA be completely depleted within 10 years.

OTHER TYPES OF BENEFICIARIES (ESTATES, TRUSTS, CHARITIES, ETC.)

The withdrawal options available for other types of beneficiaries such as estates, trusts, and charities can be quite complex depending on the type of IRA, the type of beneficiary, and the timing of the IRA owner's death. Nonetheless, there are frequently options available that can allow these types of beneficiaries to extend the taxsheltered benefits of Inherited IRAs.

[1] In multiple-primary beneficiary scenarios, an Eligible Designated Beneficiary may be forced to deplete the IRA within 10 years if their interest has not been separately accounted for by December 31 of the year following the year of the IRA owner's death.