

## Moving an Inherited IRA

**Take-Away:** Non-spouse beneficiaries have limited options for moving their inherited IRA or qualified plan account. Using the wrong method can result in a loss of opportunities for the beneficiary's efficient tax planning for those distributions.

**Background:** Lots of questions these days surround inherited retirement accounts, thanks in large part to the SECURE Act. Much of the confusion has been caused by the major change in distribution rules under the SECURE Act, and less so with the SECURE Act 2.0.

The objective of many beneficiaries who inherit a retirement account is to let that inherited account grow as long as possible tax-deferred and only take required minimum distributions (RMDs.) With the SECURE Act, depending upon whether the inheritor is an *eligible designated beneficiary*, or not, that tax-deferred growth can continue for up to 10 years. Unfortunately, moving the inherited retirement account incorrectly by its designated beneficiary can result in unintended distributions and therefore they will lose the opportunity for tax-deferred growth in their inherited retirement account.

**Safest Transfer:** To enable the continued tax deferral of the inherited retirement account, the safest way to move the inherited account from one IRA custodian to another IRA custodian is the direct transfer method. The issuing IRA custodian of the retirement account must make the asset payable to the receiving IRA custodian as it is titled. Neither IRA custodian should report the direct transfer to the IRS. Both individuals and nonperson beneficiaries, (like a trust, estate, or charity) may transfer their inherited IRAs to a 'beneficiary' IRA. This includes traditional IRAs, SEP IRAs, Roth IRAs, and in some cases SIMPLE IRAs. With a SIMPLE IRA (*a savings incentive match plan for employees*) if the SIMPLE IRA has been funded for at least two year this direct transfer rule will apply. If that is not the case, then an inherited SIMPLE IRA will need to remain in a 'beneficiary' SIMPLE IRA until the two-year holding requirement has been met.

**Transfer Mistake:** If the beneficiary who inherited the retirement account takes a distribution, that distribution must be included in the beneficiary's taxable income for the year of distribution, i.e., the tax deferral will be lost. One common mistake that is made that that non-spouse designated beneficiaries cannot *roll over* the distribution taken from an inherited retirement account.

Example: In 2024, 49-year-old Ned inherited a Roth IRA from his aunt Sally, who died when she was age 70. Sally's Roth IRA had a balance of \$500,000 at the time of her death. Ned is the designated beneficiary of Sally's Roth IRA; Ned is not an *eligible designated beneficiary*, meaning that he is neither disabled nor chronically ill. Consequently, Ned has 10 years to distribute the inherited Roth IRA, before 2034. Taking any distributions from the inherited Roth IRA is optional for Ned. Ned can allow the Roth IRA earnings to be tax-free, providing to him with a tax-free growth, leading to a \$783,575 balance in the Roth IRA in 2034 if the \$500,000 Roth IRA enjoys a rate of return of 7% for the next 10 years. Ned wants to use a Roth IRA custodian other than the one that Sally used. Ned contacted Sally's Roth IRA provider and told it that he wanted to roll over the inherited Roth IRA. That IRA custodian had Ned complete a distribution request form and gave Ned a check for \$500,000. Yet Ned is a non-spouse beneficiary; the \$500,000 that he received in Sally's Roth IRA cannot be rolled over to the new Roth IRA custodian. The upshot is that Ned will lose the potential tax-free growth of \$283,575 over the next 10 years. Ned should have told Sally's Roth IRA custodian that he wanted a direct transfer of Sally's Roth IRA that he inherited and request the direct transfer of it on Ned's behalf to Ned's selected (new) Roth IRA custodian.

Qualified Plans: If a 401(k) account or other qualified employer plan account, e.g., a 403(b) or 457(b) plan, is inherited it can be rolled over to a 'beneficiary' IRA. Again, it must be done as a direct rollover—there is no 60-day rollover option. A direct rollover from an employer's qualified plan occurs when the plan administrator pays the distribution to a 'beneficiary' IRA that is registered in part, in the name of the beneficiary. If the retirement account balance is directly paid to the beneficiary, it cannot be rolled over by the beneficiary. Such a rollover (indirect rollover—where the assets are paid to the individual beneficiary who then rolls over the amount to his/her own IRA) is only available to a surviving spouse beneficiary. Neither a direct rollover nor an indirect rollover is available to a nonperson beneficiary. If the beneficiary is the decedent's estate, any distributions must be made to the estate, never to a 'beneficiary' IRA that is opened by the estate. Note that if a traditional employer qualified plan account, e.g., a 401(k) account, is transferred to an inherited Roth IRA, any pretax amount is taxable and included in the beneficiary's income for the year of the transfer.

RMDs: Any required minimum distribution (RMD) due to the participant or IRA owner must be taken *before* the rollover to a 'beneficiary' IRA. The undistributed RMD amount that is not taken cannot be included in any rollover amount to the inherited 'beneficiary' IRA.

Registering the "Beneficiary" IRA: The 'beneficiary' IRA must be registered in both the name of the beneficiary and the name of the retirement account owner. This registration enables the IRS to know from whom the beneficiary inherited the IRA or retirement account.

Examples: Kristen White inherited an IRA from her uncle Oliver Black. Greenleaf Trust is the IRA custodian. The registration of Kristen's inherited IRA would be IRA FBO Kristen White as Beneficiary of Oliver Black, Greenleaf Trust as custodian.

Or the 'beneficiary' IRA might be registered as IRA FBO Oliver Black (Deceased) Kristen White (Beneficiary) Greenleaf Trust (Custodian)

In short, there is some latitude in how the 'beneficiary' IRA is registered.

If Oliver Black had named his estate as the beneficiary of his IRA, in other words a nonperson, and acceptable title would be IRA FBO, The Estate of Oliver Black, Greenleaf Trust as custodian.

Conclusion: The big mistake is in assuming that all inherited retirement accounts can be rolled over to the beneficiary and then to the inherited 'beneficiary' IRA. There is no 60-day rollover option. Only surviving spouses can engage in a roll over to the survivor's own retirement account. Using the wrong method to move an inherited retirement account will result in unintended distributions and cause the beneficiary to lose opportunities to obtain tax-deferred growth in the inherited retirement account.