

INHERITING AN IRA CAN BE TRICKY

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Inheriting an IRA can be tricky. If you don't understand the inheritance rules, you could make costly mistakes. Here are some simple guidelines.

Spousal Rules

A surviving spouse has three options when inheriting an IRA from a deceased spouse:

- Cash in the IRA and pay income tax on the withdrawal
- Leave the IRA in the deceased's name
- Roll it over into an IRA account in the survivor's name

The decision may depend on the survivor's age, the age of the IRA owner at the time of death, whether withdrawals had already begun, income requirements, and other financial circumstances. Let's look at two situations:

Learn all you can from the mistakes of others. You won't have time to make them all yourself.

Alfred Sheinwold

Inheriting spouse under age 59 ½

If the survivor leaves the IRA in the deceased's name, he or she can make withdrawals before age 59 ½ without paying the 10% early withdrawal penalty, though ordinary income taxes will still be due. If the survivor rolls the IRA into his or her own IRA, then early withdrawals may be subject to the penalty plus ordinary taxes.

Inheriting spouse over age 59 ½

In this case, it usually makes more sense to roll the IRA over into the survivor's own IRA as it's easier to manage, allows them to name new beneficiaries, and allows those new beneficiaries to "stretch" distributions when they inherit. For survivors younger than 70 ½, there can be an additional benefit. If the deceased had already begun taking required minimum distributions, the inheriting spouse must continue this based on what would have been the deceased's life

expectancy. By rolling the IRA over into the survivor's own IRA, distributions can be delayed until shortly after the survivor turns 70 ½ and will be based on the survivor's life expectancy.

Non-spouse Rules More Limiting

If distributions had already started and there is no designated beneficiary, the heir must continue withdrawals based on the owner's remaining single life expectancy at death. If distributions had not started, the heir must take all the money out within five years and pay ordinary income taxes. However, there's no early withdrawal penalty, even if the heir is younger than 59 ½.

Designated non-spouse beneficiaries can take annual minimum withdrawals based on their own life expectancy, regardless of whether distributions had already started. Non-spouses cannot roll an inherited IRA into their own, but by establishing a "beneficiary IRA" (known as a stretch IRA, dynasty IRA or legacy IRA) the inherited IRA remains in the name of the deceased, benefiting the heir.

Multiple non-spouse heirs can split the inherited IRA into separate IRAs. If they don't split it, minimum withdrawals are based on the life expectancy of the oldest heir.

It's best not to make any decisions before consulting a financial professional who is very familiar with the inheritance rules. Since not all IRA custodians allow all of these federally recognized options, you may need to change custodians. If you would like more information on IRA distribution rules, please call us at (405) 607-4820 to request articles we've written for the Oklahoma Society of CPAs.

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