4 STEPS TO TAKE WHEN YOU INHERIT AN IRA

As the population in the U.S. grows older, it is becoming increasingly common for individuals to inherit retirement accounts from their family members or dear ones. However, it's important that as an heir to such accounts you follow particular steps in order to avoid making mistakes that could cost you.

There are several options to handling inherited accounts, which depend on a variety of factors including your relationship to the original account holder, the age of the original account holder when they passed away and the type of account you've inherited. Here are four crucial steps to follow to increase your benefits in the long run:

Step 1: Title the New IRA

Once you inherit an IRA, you'll want to make sure it's set up correctly. An inherited IRA should have the name of the deceased original owner and it should also indicate that the IRA was inherited. Alternatively, if the deceased was a spouse you have the option to roll over the amount of the inherited IRA into your account. Keep in mind that if you transfer any distributed money to a new account in your name, you must do so within 60 days. (1)

If you've inhertied an IRA from someone other than a spouse, you will not be able to simply move money into your own retirement account. In order to keep the tax benefits of the inherited account, you will need to set up a new Inherited IRA for Benefit under your name. (2) After the account has been created, you'll be able to transfer assets from the original account to your beneficiary IRA.

Step 2: Calculating the Right Distribution Amount

If you're the spouse of the deceased, the prior year-end account value and life expectancy are needed to calculate distribution amount on your inherited IRA. For this calculation, the value of the account from the last year is used. For example, in order to calculate distributions for the year 2026, the value on December 31, 2025 is used.

If you are a non-spousal beneficiary, it's important to note that you'll be required to withdraw the entirety of the account within 10 years, if the deceased passed on or after January 1, 2020. (3) (Prior to the SECURE Act passing, the IRA amount was allowed to be withdrawn throughout the beneficiary's remaining life expectancy.)

Step 3: Determine if the IRA Has an After-Tax Basis

Many beneficiaries are unaware if the IRA they've inherited has an after-tax contribution you should fill out a Form 8606. (4) By completing this form you'll be able to claim the non-deductible portion of the Required Minimum Distribution.

You can always ask the executor if they are aware that the IRA has an after-tax contribution, but they might not know themselves and will need to refer to the tax returns of the deceased to learn if they filled out the form previously.

Step 4: Make a Plan for the Taxation of Distributions

Tax of distribution is different for Roth IRAs and other IRAs. In many cases, Roth IRAs have distributions that are tax-free if the beneficiary is taking the minimum distributions. However, for other IRAs, the distributions are fully taxable unless the original IRA owner had a tax basis on their IRA. If the distribution is taxable, you can add the taxable portion of the distribution to the tax projection for the year to learn the amount of tax you should withhold.

The 10-Year Rule

As you make a plan for distribution, remember the SECURE Act's change for non-spousal beneficiaries. The 10-year rule, established by the SECURE Act of 2019, requires most non-spouse beneficiaries to fully withdraw all assets from an inherited IRA by December 31 of the 10th year following the original owner's death. Exceptions to this rule include:

- Disabled or chronically ill persons
- Minors
- Those who are less than 10 years younger than the deceased (3)

If the original owner died after their Required Beginning Date (RBD) for taking their own RMDs, the beneficiary must take annual required minimum distributions (RMDs) in years 1-9, with the remaining balance withdrawn in year 10 before December 31st. Failing to withdraw the funds on time can result in a 25% penalty on the amount that should have been withdrawn.

A required minimum distributions (RMD) is the mandatory, taxable minimum amount you must withdraw annually from tax-deferred retirement accounts. The required beginning date (RBD) is generally April 1 of the year following the year you turn age 73 (for those turning 72 after Dec 31, 2022).

To avoid making costly errors, you should meet with your retirement wealth advisor as soon as you learn that you have inherited an IRA. Mistakes could mean larger taxes and complexities in the long run.

(1) https://www.irs.gov/retirement-plans/plan-participant-employee/rollovers-of-retirement-plan-and-ira-distributions

(2) https://www.forbes.com/sites/davidrae/2019/09/19/inheriting-an-ira/#6993dff82b7f

(3)https://www.congress.gov/bill/116th-congress/house-bill/1994/text?q=%7B%22search%22%#A%5B%22h.r+1994%22%5D%7D&r=1&s=2#toc-H084B5EBD76DF47c0B895121999E2270E

(4) https://www.investopedia.com/articles/retirement/04/030304.asp

Monique@LBDIAS.com www.LBDIAS.com 714-541-4180