Brentmark

Nicole L. Maholtz
President & CEO
P.O. Box 3
Cooksburg, PA 16217-0003
(803) 781-9595 opt 1
Nicole@brentmark.com
www.brentmark.com

2020 IRA Beneficiary Checklist: SECURE Act Transition Included

For Beneficiaries that Inherit IRAs by December 31, 2019

Protect inherited IRAs from unintended tax consequences and penalties

Baby boomers own a significant portion of the $30.0 trillion[1] held in retirement accounts[2]. Much of this will be passed on to beneficiaries who have limited options of continuing the tax-deferred status of those assets. Making the right moves can allow beneficiaries to implement distribution strategies to minimize income taxes and avoid excise taxes.

Summary of IRA Beneficiary Distribution Options

The primary factors that determine the distribution options available to beneficiaries are: **(1)** whether the IRA owner died before the required beginning date (RBD), which is when required minimum distributions (RMDs) must begin; and **(2)**, the beneficiary status, which is determined by whether the surviving spouse is the sole primary beneficiary, a nonspouse beneficiary or spouse who is not the sole primary beneficiary, or a nonperson beneficiary, and, **(3)** whether the IRA owner died before January 1, 2020. The following tables provides a high-level summary.

Quick Reference: IRA Beneficiary Distribution Options When the IRA Owner died before January 1, 2020

Beneficiary	When IRA owner dies before the RBD	When IRA owner dies on/after the RBD
When the spouse is the sole beneficiary, he/she may:	▪ Transfer or roll over to own IRA ▪ Rollover to own qualified plan such as a 401(k), 403(b), 403(a) or governmental 457(b) plan. Only if permitted by the plan. **N/A for Roth IRAs** ▪ Keep in a Beneficiary IRA and take life expectancy payments**:** Distributions would be taken over the *recalculated* single life expectancy of the surviving spouse, beginning by the <u>later of</u>: **(a)** 12/31 of the year following the year in which the IRA owner dies, **or** **(b)** 12/31 of the year the IRA owner would have reached age 70 ½ ▪ **5-Year Rule:** Distributions are optional, until December 31 of the 5th year following the year in which the IRA owner dies, at which time the entire balance must be distributed	▪ Transfer or rollover to own IRA ▪ Rollover to own qualified plan, 403(b), 403(a) or governmental 457(b) plan. ▪ Keep in a Beneficiary IRA and take life expectancy payments: Beginning by 12/31 of the year following the year in which the IRA owner dies, over the <u>longer of</u>: ○ The remaining *nonrecalculated* life expectancy of the deceased IRA owner, or ○ The *recalculated* life expectancy of the surviving spouse. Because Roth IRA owners are not subject to the RMD rules, there is no RBD for Roth IRAs. Therefore, the distribution options for Roth IRAs are usually the same as those that apply to a Traditional IRA when the Traditional IRA owner dies before the RBD.
Nonspouse beneficiary he/she may:	▪ Spouse beneficiary only: Rollover to own qualified plan such as a 401(k), 403(b), 403(a) or governmental 457(b) plan. Only if permitted by the plan. **N/A for Roth IRAs** ▪ Keep in a Beneficiary IRA and take life expectancy payments**:** Distributions would be taken over the *nonrecalculated* single life expectancy of the beneficiary, beginning by 12/31 of the year following the year in which the IRA owner dies. ▪ **5-Year Rule:** See above for explanation of the 5-year rule	▪ Keep in a Beneficiary IRA and take life expectancy payments: Beginning by 12/31 of the year following the year in which the IRA owner dies, over the <u>longer of</u>: ○ The remaining *nonrecalculated* life expectancy of the deceased IRA owner, or ○ The *nonrecalculated* life expectancy of the beneficiary

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[1] ICI's Quarterly Retirement Market Data, Third Quarter 2019.
[2] Center for Retirement Research, Boston "401(K)/IRA HOLDINGS IN 2016: AN UPDATE FROM THE SCF,":

Beneficiary	When IRA owner dies before the RBD	When IRA owner dies on/after the RBD
A nonperson beneficiary: example estate, charity, **may:**	Take distributions under the 5-year rule	Keep the assets in an inherited IRA and take distributions over the decedent's remaining life expectancy beginning by 12/31 of the year following the year in which the IRA owner died

Note: Special rules apply when a trust is the beneficiary, depending on whether the trust is qualified or nonqualified.

Beneficiary Checklist

One seemingly simple mistake can cause a beneficiary to lose tax benefits, owe penalties to the IRS, or take a distribution they didn't intend to take. Prevent errors by using this checklist when handling inherited IRAs:

- ✓ **Determine date of death of the IRA owner**. Knowing when the IRA owner died is the first step in determining whether the beneficiary is still within deadlines for completing certain tasks, including determining who is the true designated beneficiary, if any.
- ✓ **Check the calendar of beneficiary dates and determine which might be applicable to your client for any required action.** These are as follows:
  - ***Nine months after the date the IRA owner died, or if later, nine months after the beneficiary reaches age 21. Deadline to disclaim an inherited IRA:*** The disclaimer is valid only if it is received by the IRA custodian by the nine-month deadline. Other requirements must also be met. These are explained in Internal Revenue Code § 2518. An attorney should be consulted to determine if additional requirements apply under state law.
  - ***September 30 of the year following the year the IRA owner dies: Deadline to determine designated beneficiaries whose life expectancy can be used to calculate post-death distributions***. If there are multiple beneficiaries of an IRA, the oldest beneficiary's life expectancy is used, unless separate accounting occurs by December 31 of the year following the year in which the IRA owner dies. This applies only to beneficiaries who remain[3] after the September 30 deadline. Beneficiaries that properly disclaim or distribute their full share by the September 30 deadline are disregarded for the purposes of determining if the IRA owner is survived by a designated beneficiary.
  - ***October 31 of the year following the year the IRA owner dies: Deadline by which trust documentation for a qualified/valid trust must be provided to the IRA custodian.*** If a trust satisfies the requirements as described under Treas. Reg. 1.401(a)(9)-4, A-5(b)), a copy of the trust or qualifying documentation must be provided to the IRA custodian by the October 31 deadline, and must show the beneficiaries on record as of the September 30 deadline.
  - ***December 31 of the year following the year the IRA owner dies. Deadline for separate accounting when there are multiple beneficiaries***. Separate accounting by this deadline allows each beneficiary to use their own life expectancies. If separate accounting does not occur by this deadline, the life expectancy of the oldest beneficiary must be used to determine post death RMD amounts. Only beneficiaries that remain[3] after the September 30 deadline are taken into consideration for this purpose.
- ✓ **Contact the IRA custodian regarding operational and documentation policies.** These requirements vary among custodians. Some will take instructions over the telephone, and some require physical paperwork. The key here is to ensure that any paperwork completed by the beneficiary will produce the intended results.
  A common mistake is for a beneficiary to complete a distribution form when the intent was to transfer the assets from one inherited IRA to another. To prevent this from occurring, remind beneficiaries to work with an advisor who is proficient in the area of IRA beneficiary planning.
- ✓ **Determine distribution options applicable to the beneficiary.** The table on the first page provides a high-level summary of the distribution options that are available to beneficiaries. However, an IRA agreement can include more restrictive provisions. Additionally, IRA agreements typically include default elections, some of which the beneficiary can override if timely elections are made. It is therefore important to check an IRA agreement to determine which options are available to your client, and, if those are more restrictive than the options available under the regulations, determine how they can be overridden. Some can be overridden with an election.
- ✓ **Look for special planning opportunities for spouse beneficiaries**. The distribution options that are available to spouse beneficiaries are more flexible than those that apply to other beneficiaries. For example, the spouse beneficiary can transfer/rollover an inherited IRA to his/her own IRA or other retirement account. If a spouse beneficiary is under the age of 59 ½, and will be taking distributions from the inherited amount before reaching age 59 ½, consider whether it makes better tax sense to keep the assets in an inherited IRA, which would exempt distributions from the 10% early distribution penalty.
- ✓ **Ensure that beneficiary RMDs are taken by the deadline.** RMDs that are not taken by the deadline are subject to a 50% excess accumulation penalty. The IRS will waive this penalty if the deadline was missed due to reasonable cause.

Some mistakes that are made with inherited IRAs cannot be fixed. Working with a comprehensive checklist can help to avoid such mistakes. The items provided in this checklist are only some of those that should be part of a beneficiary checklist.

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[3] Beneficiaries who have not disclaimed or distributed their share of the inherited account