

## **Inheriting an IRA--What You Need to Know**

The rules governing inherited IRAs can be complicated. Here are the major issues to consider.

### **Transferring inherited IRA assets**

If you inherit a traditional or Roth IRA from someone who isn't your spouse, your options are fairly limited. You can't roll the proceeds over to your own IRA, treat the IRA as your own, or make any additional contributions to the IRA. What you can do is transfer the assets to a different IRA provider, as long as the registration of the account continues to reflect that the IRA is an inherited IRA, and not your own.

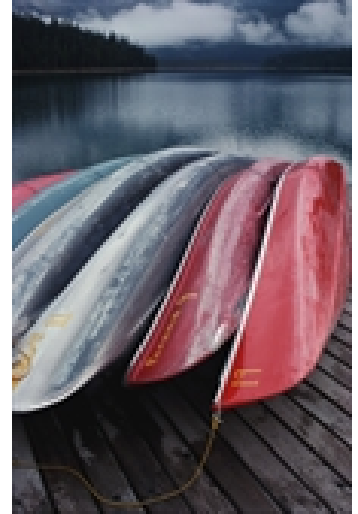
If you inherit an IRA from your spouse, however, you have additional options. You can roll over all or part of the IRA proceeds to your own IRA (or to a qualified plan). If you roll the proceeds over to your own IRA (an existing one, or one you establish just for this purpose) the rules that apply to IRA owners, not beneficiaries, will apply from that point on. If you're the sole beneficiary, you can also generally treat the inherited IRA as your own by simply retitling the IRA in your name.

But you aren't required to assume ownership of an IRA you inherit from your spouse. You can, instead, continue to maintain the inherited IRA as a beneficiary. You might want to do this if, for example, you inherit a traditional IRA and you'll need to use the funds before you turn 59½ (distributions from inherited IRAs aren't subject to the 10% early distribution penalty but distributions from IRAs you own are subject to the penalty, unless an exception applies).

A spouse beneficiary can also convert all or part of an inherited traditional IRA to a Roth IRA (you'll generally have to pay income tax on the amount converted). This option is not available to nonspouse beneficiaries.

### **Required minimum distributions**

*Nonspouse beneficiary:* Federal law requires that you begin taking distributions (called required minimum distributions, or RMDs) from an inherited IRA (traditional or Roth) after the IRA owner dies.



***The rules governing inherited IRAs can be complicated. If you inherit an IRA from someone who isn't your spouse, your options are fairly limited. If you inherit an IRA from your spouse, you have many more options.***

*Spouse beneficiary:* If you roll the inherited IRA over to your own IRA, or treat it as your own, then the RMD rules apply to you the same way they apply to any IRA owner--you'll generally need to begin taking RMDs from a traditional IRA after you turn 70½; no lifetime RMDs are required at all from a Roth IRA. If you don't roll the IRA assets over or treat the IRA as your own, then the same rules described above for nonspouse beneficiaries generally apply to you, except that you can defer receiving distributions until your spouse would have turned 70½.

**Note:** *In both cases, if the IRA owner died after turning 70½ and didn't take a required distribution for the year of death, you'll need to make sure to take that distribution by December 31 of the year of death in order to avoid a 50% penalty.*

### **Taxation of inherited Roth IRAs**

Qualified distributions to a beneficiary from an inherited Roth IRA are free from federal income taxes. To be qualified, the distribution must be made after a five-year holding period. The five-year period begins on January 1 of the year the deceased IRA owner first established *any* Roth IRA, and ends after five full calendar years. If you take a distribution from an inherited Roth IRA before this five-year period ends, any earnings you receive will be nonqualified, and will be subject to federal income taxes (earnings generally come out last).

For example, you inherit a Roth IRA from your father on January 1, 2013. Your father established this IRA in June 2012. Your father also established a separate Roth IRA, which you did not inherit, in December 2008. Distributions you receive from the Roth IRA will be qualified, and tax free, because the five-year holding period (January 1, 2008, to December 31, 2012) has been satisfied.

If you're a spouse beneficiary, and you roll the inherited Roth IRA over to your own Roth IRA or treat the inherited IRA as your own, then you'll be eligible to take tax-free distributions only after *you* reach age 59½, become disabled, or have qualifying first-time homebuyer expenses. You'll also need to satisfy the five-year holding period, but a special rule applies. The five-year period for all of your Roth IRAs--including the inherited IRA--will be deemed to have started on January 1 of the year either you or your spouse first established *any* Roth IRA.

## **Speak to a financial professional if ...**

- You're sharing the inherited IRA with other beneficiaries. This can impact when and how you must begin receiving RMDs from the IRA.
- You don't want or need the IRA funds. You may be able to disclaim the IRA and have it pass to another beneficiary. This must be done in accordance with strict IRA rules.
- Any estate taxes were paid that are attributable to the inherited IRA. You may be entitled to an income tax deduction equal to the estate taxes paid.

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