Traditional IRAs

The Inherited Traditional IRA –

When the IRA Owner Dies on or After January 1, 2020

Questions & Answers

Purpose

This brochure explains the features of an Inherited traditional IRA. As will be illustrated, the person who has "inherited" a traditional IRA has indeed acquired a very valuable gift. If you are such a beneficiary, you will want to understand the tax rules.

A person establishes and maintains a traditional IRA to realize certain tax benefits. A person is able to designate a person or legal entity to take over the "ownership" of these traditional IRA funds after his or her death. Once the original traditional IRA accountholder dies, this traditional IRA becomes an Inherited traditional IRA. The person who was designated as the beneficiary "inherits" this traditional IRA. The traditional IRA custodian now owns this traditional IRA on behalf of the beneficiary rather than the original accountholder.

After an IRA accountholder dies, there are rules called RMD beneficiary rules which mandate that the IRA funds be distributed to the beneficiary(ies) on or before certain time deadlines.

A primary benefit of a traditional IRA including an inherited IRA is, any income earned within the traditional IRA is not presently taxed. The income and certain contributions will be taxed when withdrawn in future years.

This brochure discusses the general rules for non-spouse beneficiaries such as children, grandchildren or other persons. There is only limited discussion of when a spouse is a beneficiary because most spouse beneficiaries will elect to treat their deceased spouse's IRA as their own IRA. An inherited IRA ceases to be an inherited IRA when a spouse beneficiary makes the election or takes a distribution and rolls it over into his or her own IRA.

What are the tax consequences of my being a beneficiary to a traditional IRA?

The general tax rule is, the recipient of an IRA distribution, including an IRA beneficiary, is required to include that distribution in income and will pay tax at his or her marginal tax rate. If there is basis within the IRA, the withdrawn amount attributable to basis is not included in their income. The 10% pre-59½ additional tax is never owed by a beneficiary. The standard income tax withholding rules applying to an IRA distribution apply. In order to determine if there is basis within the IRA you will need to review the personal tax and IRA files of the deceased IRA owner.

Another general IRA tax rule is – a person in applying the IRA distribution rules must aggregate all traditional IRAs, SEP-IRAs and SIMPLE-IRAs. However, a beneficiary is only allowed to aggregate IRAs acquired from the same deceased IRA owner. No income taxes are owed until a distribution is made to a beneficiary.

Why do I as a beneficiary need to be concerned about the 10% or the 25% excess accumulations tax?

A beneficiary who fails to withdraw their annual RMD by the appropriate deadline will owe the 10% or the 25% excess accumulations tax.

What if I am the designated beneficiary of my spouse's traditional IRA?

As a spouse beneficiary you are an EDB. In general, you have three options, You may elect to treated your deceased spouse's traditional IRA as your own traditional IRA. Or you may use the life distribution rule or when applicable the 10-year rule. Almost always you as a surviving spouse will elect to treat your deceased spouse's traditional IRA as your own because then you are not required to withdraw any amount until the year you attain age 73.

A spouse beneficiary is eligible to use the 10-year rule only if their deceased spouse died before their required beginning date.

Have the RMD rules for certain beneficiaries changed?

Yes. With the enactment of the SECURE Act within the Further Consolidations Act of 2020 there are now different rules depending upon whether the traditional IRA owner died before January 1, 2020 or on or after January 1, 2020 and whether the beneficiary is an Eligible Designated Beneficiary (EDB) or not an EDB.

What rules apply for the year the IRA accountholder dies?

If the IRA accountholder died before his or her required beginning date, there is no RMD which must be distributed for such year. If the IRA accountholder died after his or her required beginning date, the RMD as determined for the IRA accountholder must be distributed for such year. To the extent this amount was not paid out to the IRA accountholder before his or her death, the beneficiary(ies) will need to be paid their proportionate share of the RMD by December 31, or the 10% or 25% tax will apply.

What is the concept of the new laws applying to IRA beneficiaries?

Under the old law (the IRA accountholder died before 2020) most beneficiaries were able to spread out distributions over their life expectancy and continue to have taxes deferred if that is what they wanted. Under the new law (the IRA accountholder dies after 2019) most beneficiaries are now required to close the inherited IRA within 10 years. Continued tax deferral is limited to 10 years. However, beneficiaries who qualify as an Eligible Designated Beneficiary (EDB) still are able to spread out distributions over their life expectancy and continue to have taxes deferred for a longer period.

Must I determine if I am an EDB or a non-EDB?

Yes.

Must I determine if the IRA accountholder died before or on/after their required beginning date?

Yes.

Who is a non-EDB beneficiary?

You are a beneficiary who is more than 10 years younger than the deceased IRA accountholder, who is not disabled, who is not chronically ill or who is not a minor child of the deceased IRA accountholder.

Who is an EDB beneficiary?

You are a beneficiary who is not more than 10 years younger than the deceased IRA accountholder, who is disabled, who is chronically ill or who is a minor child of the deceased IRA accountholder. An EDB is also a surviving spouse beneficiary or a non-spouse beneficiary of an IRA accountholder who died before 2020.

What RMD Rule applies to a non-EDB beneficiary when the IRA accountholder died before their required beginning date?

This non-EDB beneficiary who is a living person must close the inherited IRA under the 10-year rule. Under the 10-year rule the only requirement is to close the inherited IRA by December 31 of the 10th year.

It is permissible to have no withdrawals for years 1-9. Many beneficiaries will want to withdraw approximately 10% each year for income tax planning reasons.

What RMD rule applies to a non-EDB beneficiary when the IRA accountholder died after their required beginning date?

This non-EDB beneficiary who is a person must close the inherited IRA under the standard beneficiary life distribution rule, but it must also be closed under the 10-year rule. An example is set forth below. Jane Doe, age 58 in 2021, is the beneficiary of Mary Doe's IRA. Mary was age 81 when she died in 2021. Jane must commence RMD distributions in 2022 and close the inherited IRA by December 31, 2031. See below.

Year	Jane's Age	RMD Divisor	Closeout Deadline
2022	59	28.0	
2023	60	27.0	
2024	61	26.0	
2025	62	25.0	
2026	63	24.0	
2027	64	23.0	
2028	65	22.0	
2029	66	21.0	
2030	67	20.0	
2031	68	1.0	12/31/2031

Note. Although the law permits a beneficiary to only withdraw the RMD for years 1-9, many beneficiaries will decide for tax reasons to take equal (or nearly equal) distributions over the 10 year period.

What RMD rule applies to a beneficiary who qualifies as an EDB and the IRA account- holder died <u>before</u> their required beginning date?

An EDB has two options with respect to the inherited IRA. There is no right to treat as his or her own. Option one is to use the standard life distribution rule. Option two is to use the 10-year rule. Once made the election is irrevocable.

The standard life distribution rule is - the annual RMD equals the fair market value as of the preceding December 31 divided by a divisor from the Single Life Table. The initial divisor for the first year after the IRA accountholder died is determined using the age of the beneficiary in that year and the Single Life Table. For subsequent year subtract 1.0 for each elapsed year.

Under the 10-year rule the only requirement is to close the inherited IRA by December 31 of the 10th year.

A beneficiary will be an EDB if as of the day the I RA accountholder dies the beneficiary is: more than ten years younger than the IRA accountholder, disabled, chronically ill, or a child of the IRA accountholder who is not yet age 21. The beneficiary will need to certify if he or she is an EDB and assume full responsibility for the certification.

What RMD rule applies to a beneficiary who qualifies as an EDB and the IRA account-holder died <u>after</u> their required beginning date?

This non-spouse beneficiary will use the standard life distribution rule. It will be used for as long as the non-spouse beneficiary lives. Upon the beneficiary's death the subsequent beneficiary must continue the distribution schedule but close it under the 10-year rule.

The standard life distribution rule is - the annual RMD equals the fair market value as of the preceding December 31 divided by a divisor from the Single Life Table. The initial divisor for the first year after the IRA accountholder died is determined using the age of the beneficiary in that year and the Single Life Table. For subsequent year subtract 1.0 for each elapsed year.

What is the general RMD formula for an IRA beneficiary entitled to use the life distribution rule?

It is the same formula which applies to a living IRA accountholder, except the life-expectancy table to be used is different. An IRA beneficiary uses the Single Life Table. An IRA beneficiary never uses either the Uniform Lifetime Table or the Joint and Last Survivor Table.
The Formula for Current Year:
12-31-XX of Preceding Year divided by the Period from Single Life Table (As Adjusted) equals RMD.

How is the beneficiary's divisor determined?

The Single Life Table is used. Step one is to determine the age of the beneficiary in the year following the death of the IRA owner. Using this age the initial divisor is determined from the Single Life Table.

For each subsequent year, subtract 1.0 from the prior year's divisor. Note for subsequent years you do not redetermine the divisor based on your current age. A special rule applies to a spouse beneficiary who is the sole primary beneficiary.

Single Life Table

Age of IRA Beneficiary	Distribution Period (in yrs)	Age of IRA Beneficiary	Distribution Period (in yrs)	Age of IRA Beneficiary	Distribution Period (in yrs)	Age of IRA Beneficiary	Distribution Period (in yrs)
0	84.6	31	54.4	61	26.2	91	5.3
1	83.7	32	53.4	62	25.4	92	4.9
2	82.8	33	52.5	63	24.5	93	4.6
3	81.8	34	51.5	64	23.6	94	4.3
4	80.8	35	50.5	65	22.9	95	4.0
5	79.8	36	49.6	66	22.0	96	3.7
6	78.8	37	48.6	67	21.2	97	3.4
7	77.9	38	47.7	68	20.4	98	3.2
8	76.9	39	46.7	69	19.6	99	3.0
9	75.9	40	45.7	70	18.8	100	2.8
10	74.9	41	44.8	71	18.0	101	2.6
11	73.9	42	43.8	72	17.2	102	2.5
12	72.9	43	42.9	73	16.4	103	2.3
13	71.9	44	41.9	74	15.6	104	2.2
14	70.9	45	41.0	75	14.8	105	2.1
15	69.9	46	40.0	76	14.1	106	2.1
16	69.0	47	39.0	77	13.3	107	2.1
17	68.0	48	38.1	78	12.6	108	2.0
18	67.0	49	37.1	79	11.9	109	2.0
19	66.0	50	36.2	80	11.2	110	2.0
20	65.0	51	35.3	81	10.5	111	2.0
21	64.1	52	34.3	82	9.9	112	2.0
22	63.1	53	33.4	83	9.3	113	1.9
23	62.1	54	32.5	84	8.7	114	1.9
24	61.1	55	31.6	85	8.1	115	1.8
25	60.2	56	30.6	86	7.6	116	1.8
26	59.2	57	29.8	87	7.1	117	1.6
27	58.2	58	28.9	88	6.6	118	1.4
28	57.3	59	28.0	89	6.1	119	1.1
29	56.3	60	27.1	90	5.7	120	1.0
30	55.3						

As a beneficiary, may I transfer my inherited IRA funds to another inherited IRA at a different IRA custodian/trustee?

Yes. If certain information is furnished and acknowledged by both IRA custodians, then you should be able to transfer the IRA you have inherited to a different IRA custodian.

Do the tax rules authorize me to take or receive a distribution from my inherited traditional IRA and roll it over to another inherited traditional IRA?

No. You as a non-spouse beneficiary have no roll over rights with respect to a traditional IRA distribution. Unless an erroneous distribution occurs on account of the IRA custodian/trustee or its agent.

Do I as an individual who inherits an Inherited traditional IRA have the right to designate my own beneficiary(ies)?

Yes. The federal income tax laws certainly permit it.

Can a person who is a beneficiary of a traditional IRA, but who also is taking required distributions from a traditional IRA, aggregate these required distributions and take the combined amount only from the traditional IRA?

No.

What happens if I, the inheriting traditional IRA beneficiary die?

If you are an EDB, then your beneficiary must close the inherited traditional IRA under the 10-year rule.

If you are not an EDB, then your beneficiary must close the inherited traditional IRA by continuing the same 10-year schedule applying to you.

Information provided in this brochure is not intended to be legal or tax advice. You should consult your attorney or tax advisor for information that relates to your circumstances.