WELLS FARGO Advisors

Inheriting an IRA as a Non-spouse Eligible Designated Beneficiary

When you inherit an IRA and are a non-spouse eligible designated beneficiary (EDB), you will have many planning and distribution considerations. Non-spouse Eligible Designated Beneficiaries are:

- Disabled or chronically ill individuals.
- Primary beneficiary of qualified “look-through" trust who is disabled or chronically ill
- Individuals not more than 10 years younger, the same age, or older than IRA owner
- Children of the IRA owner who have not reached age 21
- Non-spouse individuals who inherited a QRP from a plan participant who died before 2020[1]

Some of your decisions will be based on your current needs, but your ultimate goal may be to maximize the value of the assets you received. We have prepared this information to help you be informed so that you can avoid common mistakes and make the most of this opportunity.

Please note: if the IRA owner dies before 2020, and a non-spouse or qualified trust inherited the account, they have the life expectancy option. In some instances the five-year rule is an option.

Tax considerations

Managing the amount you will pay in taxes is one of the most important considerations when deciding how to handle distributing money from the IRA you inherited.

- Qualified distributions from the Roth IRA you inherited are tax-free. An Inherited Roth IRA offers the opportunity for tax-free compounding of potential earnings.
- Income tax, but not the IRS 10% additional tax for early or pre-59½ distributions (10% additional tax), will apply to taxable amounts when withdrawals are taken from the Traditional IRA you inherited. Larger dollar amounts can quickly put you into a higher tax bracket, whereas taking smaller distributions over time can help avoid a significant tax bill. An Inherited Traditional IRA offers the opportunity for tax-deferred compounding of potential earnings.

[1] A beneficiary of a participant of a governmental retirement plan [as defined in section 414(d)] who dies after December 31, 2021 will follow the SECURE Act rules. If these participants die on or before December 31, 2021, the pre-SECURE Act death distribution rules apply.

Beneficiary distribution options

The following tables summarize the distribution options an EDB has from an Inherited IRA if the IRA owner died either before or on or after their required beginning date (RBD), generally April 1 following the year they reach required minimum distribution (RMD) age. RMD age is generally the year the IRA owner turned age 73 (if born after 1950), 72 (if born after 6/30/1949), or 70 ½ (born before 7/1/1949).

Beneficiary category — Individual	Life expectancy	10-year rule	10-year rule with RMDs[2]	5-year rule
Eligible designated beneficiary: **Disabled or chronically ill individuals**				
- original IRA owner dies **before** RBD	X	X		
- original IRA owner dies **on or after** RBD	X		X	
Individuals not more than 10 years younger, the same age as, or older than IRA owner				
- original IRA owner dies **before** RBD	X	X		
- original IRA owner dies **on or after** RBD	X		X	
Child of the IRA owner who has not reached age of 21[3]				
- original IRA owner dies **before** RBD	X	X		
- original IRA owner dies **on or after** RBD	X		X	
Non-spouse or qualified trust beneficiary of an IRA owners who died before 2020[4]				
- original IRA owner dies **before** RBD	X			X
- original IRA owner dies **on or after** RBD	X			

Beneficiary category — Entity	Life expectancy	10-year rule	10-year rule with RMDs[2]
Eligible Designated Beneficiary: **Primary beneficiary of qualified trust[5] is an EDB**			
- original IRA owner dies **before** RBD	X	X	
- original IRA owner dies **on or after** RBD	X		X

Understanding your options

You have a few distribution options as a non-spouse EDB. It's important to note certain distribution methods preserve the IRA asset's tax-advantaged status while others do not.

- **Open an Inherited IRA** — An Inherited IRA allows you a way to keep the funds growing tax-advantaged in an IRA while taking distributions. The account titling will always refer to the deceased IRA owner with you listed as the beneficiary. Since you aren't the owner, you may not make contributions or 60-day rollover deposits to this account. The benefit of this arrangement is that you have the option to distribute the funds over a longer period of time and are taxed only on the amount included in gross income.

Inherited IRA distribution options are:

- **Life expectancy** — This option is available for both Inherited Roth and Inherited Traditional IRAs and is often referred to as the stretch IRA strategy. Stretching an IRA simply refers to the ability for a beneficiary to take just RMDs using a divisor from the IRS Single Life Table and the prior year-end IRA value on a term certain basis. Term certain means instead of using a new divisor from the table (see page 5), one is subtracted from the original divisor in each subsequent year. These RMDs will begin the year following the IRA owner's death. Individuals may always take more than the RMD, but by taking only the minimum, the rest of the money invested remains tax-advantaged over a longer time frame. If a trust is the beneficiary, taking more than the RMD is allowed by the

[2] These regulations are proposed. IRS notice 2022-53 states if these regulations are finalized, they won't be effective until published sometime in 2023. Clients should also consult their tax professional for further guidance. Review the full IRS proposal via the Federal Register if you'd like to learn more.
[3] Then they are subject to the 10-Year Rule. The account balance must be distributed by 12/31 of the 10th year after reaching age 21 (age 31).
[4] The five-year rule may be an option.
[5] The type of qualified trust (e.g. conduit or accumulation) and who the original trust beneficiary is makes a difference in how long the Inherited IRA for the trust can remain open. It also depends on if the trust that inherited the IRA has one or more than one beneficiary. Please note that Wells Fargo Advisors does not interpret the trust and the trustee should seek competent advice to determine their exact distribution options based on their situation.

IRS rules, however, the trust document may not allow this. Any RMD not taken in the year due is subject to a 25% IRS excise tax for every dollar under-distributed. This tax can be reduced to 10% if corrected within two years from the date the tax is imposed.

- Individuals will take annual RMDs based on their life expectancy.
- Qualified trusts[5], when the IRA owner died before 2020, use the age of the oldest trust beneficiary. This DOB is used until the Inherited IRA is emptied, even if that beneficiary dies before then.
- Qualified trust[5] when the IRA owner died after 2019 and the primary beneficiary is disabled or chronically ill, use that beneficiary's life expectancy.
- Minor children of the IRA owner can take RMDs based on their life expectancy until they reach age 21. Then they are subject to the 10-Year Rule.

Calculating your Inherited IRA RMDs

Non-spouse RMD Formula

$$\frac{\text{Prior Year-End Value}}{\left(\text{Single Life Table divisor for attained age in year following IRA owner's death} - \text{1 for each subsequent year}\right)} = \text{RMD}$$

Calculating first RMD hypothetical example[6]

John, who is a disabled adult child of the IRA owner, inherited his dad Ed's IRA when Ed died last year. The 12/31 value is $100,000. John will be 35 years old this year and his Single Life Table divisor is 50.5. John's RMD is $1980 ($100,000 ÷ 50.5 = $1980).

Calculating subsequent years' RMD hypothetical example

Judy inherited her sister Maxine's IRA when Maxine died three years ago. Judy was 50 two years ago and her Single Life Table divisor was 36.2. That divisor must be reduced by 2 to reflect the subsequent years (last year and this year). Therefore, the divisor for this year is 34.2. The 12/31 value is $250,000 so Judy's RMD for this year is $7,310 ($250,000 ÷ 34.2 = $7,310).

- **Ten-year rule** — This option is available for Inherited Roth and Inherited Traditional IRAs. The Inherited IRA must be emptied by the 10th year following the year of the IRA owner's death. If the IRA owner died on or after their RBD, under the proposed IRS regulations[2], the DB must take RMDs based on their life expectancy during the 10-year period. If the IRA owner died before their RBD or the IRA is a Roth, then no distributions are required before the 10th year. Depending on the size of the account you may want to spread distributions over the 10-year period.
- **Disclaim** — If you do not need or want the IRA, you can disclaim, or refuse, all or a portion of the assets, usually within nine months after the IRA owner's death. Generally, you cannot receive any benefit from the disclaimed property, such as moving the assets to an Inherited IRA. The person who disclaims is considered to have predeceased the IRA owner so you will not be able to dictate who will inherit the IRA. If the per stirpes option has been selected then the disclaimed assets will go to your lineal descendants. If not, then the IRA passes to any other named primary beneficiary(ies) or, if none, then to the named contingent beneficiary(ies). The IRA default beneficiaries may be used if there are no valid beneficiaries on file. The defaults on a Wells Fargo Clearing Services IRA are:
  - First, a surviving spouse
  - Second, surviving children (as defined under state law)
  - Third, the owner's estate
- **Lump-sum distribution** — This strategy will exhaust the entire account in one distribution, with retirement assets losing their tax-advantaged status. Taxes will be due on the taxable portion in the year received and may place you in a higher tax bracket. Once you choose to take a lump-sum distribution, it cannot be undone because contributions including 60-day IRA-to-IRA rollover contributions are not allowed in Inherited IRAs.

Common EDB strategies

A beneficiary who chooses wisely may avoid paying income taxes on an Inherited IRA all at once. Here are a few common strategies to help you understand how to best take advantage of the inherited funds.

[6] These hypothetical examples are provided for informational purposes only. Wells Fargo Advisors is not a tax or legal advisor. Be sure to consult with your own tax and legal advisors before taking any action that may have tax or legal consequences.

Stretch IRA strategy

Stretching an IRA simply refers to the ability for you to take just RMDs from both Inherited Traditional and Inherited Roth IRAs. Below is an example of the potential benefits of choosing to implement the stretch IRA strategy, instead of taking a lump-sum distribution or emptying the account in a few years. As you can see, the younger you are when you inherit the funds, the greater the potential growth of the account.

The stretch IRA concept

Total IRA distributions over beneficiary's lifetime				
		Value of IRA when inherited by beneficiary		
		$100,000	**$500,000**	**$1,000,000**
Age	**Life expectancy**	**Total projected distributions**		
20	65 years	2,032,495	10,162,475	20,324,950
30	55.3 years	1,214,945	6,074,725	12,149,450
40	45.7 years	743,286	3,716,430	7,432,860
50	36.2 years	467,351	2,336,755	4,673,510

Assumptions: RMDs only taken, 7% annual return. This chart is hypothetical and is provided for informational purposes only. It is not intended to represent any specific investment.
Please note: Stretch IRA strategies are designed for investors who will not need the money in the account for their own retirement. There is no guarantee that there will be assets remaining in the account at the time of the IRA owner's death.

Roth IRAs

Beneficiaries who inherit a Roth IRA that has been opened more than five years will receive all distributions income tax-free. So by just taking RMDs you can have potential earnings growing tax-free that could be used to help fund your own retirement.

Naming a beneficiary to your Inherited IRA

As a beneficiary, you'll want to designate your own "successor" beneficiary to your Inherited IRA. It is important to note that the Internal Revenue Code (IRC) does not let your successor start over and stretch inherited assets out over his or her own lifetime. Instead, because you are considered an EDB they will use the 10-Year Rule. If the original IRA owner died on or after their RBD, under the proposed IRS regulations[2], your successor must take RMDs based on your life expectancy using a divisor from the IRS Single Life Table and the prior year-end IRA value, on a term-certain basis during the 10-year period. If the IRA owner died before their RBD or the IRA is a Roth, then no distributions are required before the 10th year. A successor beneficiary should be named when opening an Inherited IRA as part of a complete estate plan.

Aggregating RMDs

- RMDs need to be taken separately from both Inherited Traditional and Inherited Roth IRAs in order to take advantage of the stretch IRA strategy for both accounts.
- You can aggregate RMDs from the same type of IRA you inherited as long as they are from the same IRA owner. For example, if you inherited two Traditional IRAs from your aunt, you could determine the RMD for each IRA but satisfy both RMDs from only one of the IRAs. However, if you inherited both a Traditional and Roth IRA from your aunt you would need to take an RMD from each IRA in order to stretch them over your life expectancy.
- You cannot aggregate RMDs you take as an IRA beneficiary with any RMDs you take as an IRA owner.

Key considerations

There are a few things to consider when inheriting the deceased person's IRA and managing the funds.

- The division of the deceased's account into separate Inherited IRAs is a plan-to-plan transfer and not a taxable event.
- Non-spouse beneficiaries do not have the ability to roll over an IRA they inherit to their own IRA.
- You will need to satisfy any RMD the deceased should have taken by December 31 of the year of death of the IRA owner.
- Generally, you are responsible for the portion of the deceased's RMD based on the portion of the IRA that you inherited.
- A Roth IRA owner is always considered to have died before their RBD, so they will have no RMD due in the year of death.
- You will avoid the 10% additional tax on distributions from the Inherited IRA, no matter your age, because such distributions are coded as a "death" on the 1099R tax form.
- Any RMD not taken in the year due is subject to a 25% IRS excise tax for every dollar under-distributed. This tax can be reduced to 10% if corrected within two years from the date the tax is imposed.
- Non-spouse beneficiaries cannot convert a Traditional IRA they inherit to an Inherited Roth IRA.
- Beneficiaries who chose the life expectancy option take a yearly RMD from the Inherited IRA by December 31 beginning the year following the year of death.
- Individuals may always take more than the RMD. A trustee would have to determine if the trust could take more than the RMD.

Single Life Expectancy Table[7]

Age	Life Expectancy	Age	Life Expectancy	Age	Life Expectancy	Age	Life Expectancy	Age	Life Expectancy	Age	Life Expectancy
0	84.6	20	65.0	40	45.7	60	27.1	80	11.2	100	2.8
1	83.7	21	64.1	41	44.8	61	26.2	81	10.5	101	2.6
2	82.8	22	63.1	42	43.8	62	25.4	82	9.9	102	2.5
3	81.8	23	62.1	43	42.9	63	24.5	83	9.3	103	2.3
4	80.8	24	61.1	44	41.9	64	23.7	84	8.7	104	2.2
5	79.8	25	60.2	45	41.0	65	22.9	85	8.1	105	2.1
6	78.8	26	59.2	46	40.0	66	22.0	86	7.6	106	2.1
7	77.9	27	58.2	47	39.0	67	21.2	87	7.1	107	2.1
8	76.9	28	57.3	48	38.1	68	20.4	88	6.6	108	2.0
9	75.9	29	56.3	49	37.1	69	19.6	89	6.1	109	2.0
10	74.9	30	55.3	50	36.2	70	18.8	90	5.7	110	2.0
11	73.9	31	54.4	51	35.3	71	18.0	91	5.3	111	2.0
12	72.9	32	53.4	52	34.3	72	17.2	92	4.9	112	2.0
13	71.9	33	52.5	53	33.4	73	16.4	93	4.6	113	1.9
14	70.9	34	51.5	54	32.5	74	15.6	94	4.3	114	1.9
15	69.9	35	50.5	55	31.6	75	14.8	95	4.0	115	1.8
16	69.0	36	49.6	56	30.6	76	14.1	96	3.7	116	1.8
17	68.0	37	48.6	57	29.8	77	13.3	97	3.4	117	1.6
18	67.0	38	47.7	58	28.9	78	12.6	98	3.2	118	1.4
19	66.0	39	46.7	59	28.0	79	11.9	99	3.0	119	1.1
										120+	1.0

[7] Source: IRS Publication 590b

Talk to Wells Fargo Advisors

At Wells Fargo Advisors, we understand your desire to maximize the benefits of your inheritance. It is always wise to discuss your options on how to handle your IRA inheritance with your financial advisor as well as your tax and legal advisors before executing any strategy. Please contact your financial advisor with any questions you may have. We look forward to working with you today and in the future.

With you every step of the way

Everyone has a different vision of retirement that requires a unique financial strategy. Wells Fargo Advisors can support you in your retirement planning process by providing the guidance needed to make informed choices. We will meet with you and help create a comprehensive plan that takes into account your complete financial picture. Your financial advisor will be with you every step of the way to review your progress and adapt your plan as needed. Working together, we'll design and implement a retirement plan that will help you live out your unique vision of retirement.