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## Passing an IRA to Your Spouse

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Most IRA owners name their spouse as a beneficiary of their account. Whether you are the sole beneficiary of your spouse's IRA or one of several, this is a good time to review the choices that you'll have and the rules that you must follow after your spouse's death. The IRS revamped and simplified IRA distribution rules last year and finalized them this April, but the agency retained the rules that give special treatment to surviving spouses: A spouse beneficiary remains the only beneficiary who can roll an IRA into his or her own IRA. (Of course, a surviving spouse can also let the IRA stay in the deceased owner's name.)

### **When You Are Primary Beneficiary**

The best way to handle an IRA you inherit from your spouse depends on a number of factors. (For brevity's sake, our examples assume that the surviving spouse is the wife, but the rules are the same for a husband who inherits an IRA from his wife.)

**A rollover is usually your best choice.** After your husband's death, you can roll the account into an existing IRA of your own -- or open a new one -- and name your own beneficiary. Once the transaction is complete, you are the owner. A spousal rollover generally will extend the IRA's tax-deferral benefits for the longest time and minimize required distributions. Once you are at least 59 1/2, you can withdraw from the account without penalty. If you tap the IRA before that age, a 10% early-withdrawal penalty usually applies to premature distributions, and that's in addition to income tax on the withdrawal.

If your husband was already taking required distributions from the IRA before he died, you must withdraw the amount he would have taken in the year of his death before you do the rollover.

What if you complete a spousal rollover and subsequently need money from the IRA? See if you qualify for one of the exceptions to the 10% penalty. These include incurring onerous medical bills (see IRS Publication 590, *Individual Retirement Arrangements [IRAs]*, for details and additional exceptions) and arranging to take "substantially equal periodic payments" from the IRA for five years or until you reach 59 1/2, whichever is longer ("When You Want to Dip Into an IRA Early").

**When to leave it titled in your husband's name.** If you are not yet 59 1/2 and need to withdraw from the IRA, it may be best to leave the account in your husband's name. That way, withdrawals won't trigger the 10% penalty. When required distributions begin, the amount you must withdraw is based on your single-life expectancy.

It may also be to your advantage to leave it in your husband's name if you are older than he was. As the surviving spouse, you won't have to start minimum required distributions until December

31 of the year that your husband would have turned 70 1/2. After that, you can reduce the required distributions by rolling the IRA into your own account and naming a beneficiary. Your required distributions will then be based on the uniform lifetime table.

If you are younger than your deceased husband and leave the account in his name, mandatory withdrawals must begin no later than April 1 of the year after you turn 70 1/2.

Regardless of your age and whether you roll over the IRA or keep it in your spouse's name, if your husband was taking mandatory payouts from the account before he died, you must withdraw the amount he would have been required to take in the year of his death.

What if it's unclear whether or not you'll need money from the IRA? In that case, Barry Picker, a CPA from Brooklyn, N.Y., suggests either leaving the IRA in your husband's name until you reach age 59 1/2 or leaving enough in the account to meet your anticipated needs and rolling the rest into your own IRA.

Be careful that you don't inadvertently switch the ownership of the IRA until you intend to do so. For instance, if you contribute to your deceased husband's IRA, the IRS considers that action to cause a change of ownership and will treat the account as yours from the date of the contribution. You can also trigger the switch by failing to take a distribution that you are required to take as a beneficiary of his IRA.

## **Before You Act**

After the death of a spouse, take the time to review your financial and estate plans with a financial planner and estate lawyer who has experience with IRAs.

Remember that there is no deadline for making a spousal rollover; as a surviving spouse, you can do it anytime. Generally, the best way to handle this is with a direct custodian-to-custodian transfer. You can also withdraw the funds and deposit them in the new IRA within 60 days tax-free as long as the custodian agrees not to withhold any of the money for income taxes. If you miss the 60-day deadline for depositing the funds, the IRS will treat the rollover as a distribution, and you'll owe income taxes on the entire amount.

After your spouse's death, you have nine months to decide whether to disclaim all or part of your IRA inheritance. If you don't need the assets in the IRA and want to keep the IRA out of your estate when you die, disclaim all or part of it to the next named beneficiary, says Robert Keebler, a planner and CPA in Green Bay, Wis. In order to do this, your spouse must have named backup beneficiaries for the IRA.

## **How to Protect Your Spouse**

If your IRA has multiple beneficiaries, including your spouse, take steps to make sure everyone understands the rules of handling an IRA bequest after you're gone.

As a designated beneficiary, your spouse can roll over her share of the IRA, but make sure that you have specified what percentage or share of the IRA belongs to each beneficiary so that separate accounts can be created and each person can base required payouts on his or her own life expectancy. Beneficiaries should split the IRA into separate accounts by September 30 of the year after your death. Nonspouse beneficiaries must begin distributions from the IRA by December 31, but a spouse beneficiary has better options, as explained above.

Take steps to ensure that your estate plan won't accidentally cause your spouse to lose his or her special rights and wind up being treated as an ordinary beneficiary. This could occur in a situation such as the following: Say your IRA passes to a qualified terminable interest property (QTIP) trust, which names your wife as the income beneficiary and your two children from a previous marriage as remainder beneficiaries of the trust. Your spouse loses her right to a spousal rollover because she doesn't have an unlimited right to withdraw from the IRA. In addition, distributions must begin by December 31 of the year after your death and would be based on the life of expectancy of the oldest beneficiary, in this case, your wife. Finally, in order for the QTIP to qualify for the marital deduction -- which allows you to give an unlimited amount of property to your spouse free of estate and gift taxes -- the trust must provide that the spouse has the right to compel the trustee to withdraw all income from the IRA on at least an annual basis. As a result, if your spouse doesn't want undistributed income to wind up in the hands of your children, she can withdraw all the IRA's annual income over her lifetime.

### **The IRS Clarifies Two What-Ifs**

The final rules on IRA distributions describe how to determine withdrawals in the year of a divorce, or in the event your spouse, who is the IRA's designated beneficiary, dies. Under the new rules, your marital status for IRA distributions is determined to be what it was as of January 1. Any change in marital status subsequent to that date does not take effect for IRA purposes until the following year.

Suppose your wife, who is 12 years younger than you, dies this summer. She is the designated beneficiary of your IRA and you are currently taking minimum required distributions from the account each year. Because your wife was alive on January 1, 2002, the IRS considers you married for the entire year, so you can calculate your 2002 distribution (based on the value of the IRA on December 31, 2001) using the more favorable joint-and-survivor table. In 2003, assuming that you don't remarry but do name another beneficiary, you will use the uniform lifetime table to figure minimum distributions.

### **For More Information**

Barry Picker's *Guide to Retirement Distribution Planning*, which includes the new IRA rules, is \$25 plus \$1.75 shipping and handling. It also covers naming beneficiaries, using disclaimers and handling inherited accounts. To order, call 800-809-0015.

Nolo is updating its excellent book *IRAs, 401(k)s & Other Retirement Plans: Taking Your Money Out* (\$30). The new edition will be published in September. To order, call 800-728-3555, or visit [www.nolo.com](http://www.nolo.com).