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If An IRA Is Part Of Your Legacy, Here's What You Should Know

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By Scott Staton

If you're like many people, a good portion of your retirement savings is tucked away in an IRA, and the odds are you will need every penny once you put your working years behind you.

But what if it turns out you don't need that money? What if you're one of those fortunate people who has other assets that can be used to pay the bills and fund your retirement lifestyle? Instead of spending the money accumulating in your IRA, you decide to include it as part of the legacy you plan to leave to your beneficiaries.

If you take that route, there are a few things worth knowing to make sure you limit how much your heirs owe in taxes when the IRA comes into their possession and maximize the amount of inheritance, they can call their own.

- **Your heirs may face a deadline.** Adult children and many other people who inherit an IRA must empty the account within 10 years. Of course, with each withdrawal they make, taxes come due. This 10-year-empty-out-the-account requirement doesn't apply to everyone, though. Spouses, minor children, and disabled or chronically ill heirs can extend their IRA disbursements for the rest of their lives, if they so choose.

- **The timing of your last required minimum distribution makes a difference.** If your retirement savings is in a traditional IRA (or any tax-deferred account), you are subject to required minimum distributions (RMDs) when you reach age 72. In essence, that means you have to withdraw a certain amount of money each year whether you want to or not so the IRS can collect the taxes from you. What does this have to do with your beneficiaries and an IRA you leave behind? If you die early in the year, before you pay that year's RMD, the IRS still wants its money. It will fall to your beneficiaries to make sure the taxes are paid.

- **A Roth conversion can help eliminate your heirs' tax burden.** If you don't want your beneficiaries to be saddled by the tax bill you have left behind, one good option is to begin converting your traditional IRA to a Roth IRA. If the Roth account was opened at least five years before you die, then your heirs don't pay taxes when they withdraw money from the account. You, however, must pay taxes when you make the conversion, so it's best to spread the conversion out over several years to avoid a big tax hit all at once.

Finally, let's say that instead of bequeathing an IRA to someone, you are the one on the receiving end of an inherited IRA. What should you do with this sudden, possibly large chunk of money that's now in your possession?

Although you might be tempted to withdraw all that money at once, pay the taxes, and splurge on some luxury item for yourself, that's not the most prudent approach. You would be better off just stretching those withdrawals out over the 10 years because at least the money's there for you for a decade.

But you do have other options and, with the right planning, can make those withdrawals in a thoughtful manner that will benefit you the most. For example, you might time your withdrawals with your overall tax situation, drawing out more money during a low-income year and less during a high-income year when the withdrawal could bump you into a higher tax bracket.

You might also want to make withdrawals based on the market, shifting some of the money into other investments when the time seems opportune.

Because of the many complications involved, anyone who expects to leave an IRA as part of their legacy should seek the advice of not just a financial adviser, but also a tax professional and an estate attorney so you can make sure you're making the best decisions for your particular situation. When handled correctly, you can structure a long-lasting inheritance for your loved ones.

After all, your goal is to make sure as much of that money as possible goes to those you leave behind – and not to Uncle Sam.

About Scott Staton

Scott Staton is the founder and president of Staton Financial Group Inc. (www.statonfinancialgroup.com), an independent firm that specializes in retirement planning, income planning, 401(k) and IRA rollovers, and investment advisory services, as well as life and long-term care insurance. Staton is an Investment Adviser Representative. He holds a license for life, health and accident insurance in Oklahoma, Texas, Iowa, Kansas, and Arkansas, as well as a FINRA series 65 license in Oklahoma. He also earned his Retirement Income Certified Professional (RICP®) designation from the American College.

Investment advisory services offered through Virtue Capital Management, LLC; a SEC registered investment advisor. Virtue Capital Management is independent of Staton Financial Group, Inc.