May 2019

ED SLOTT'S IRA ADVISOR

Tax & Estate Planning For Your Retirement Savings

WHAT'S INSIDE?

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Un-Ringing the Bell: *Fixing IRA and Retirement Plan Mistakes*

It is not often that we can get a "do-over" or are able to fix an egregious mistake in the retirement-plan world. For example, if a non-spouse beneficiary of an inherited IRA attempts a rollover, there is no going back. If the money comes out, it cannot be returned; inherited IRAs can *only* be transferred. A rollover of an inherited IRA is a fatal error, and no one can un-ring that bell.

However, there are some other actions within the retirement-plan world which do carry a "get-out-of-jail free" card. Fixes can be found if you know where to look. Here are a half-dozen retirement-related mistakes that can be corrected.

NUA Distribution Fails the Lump Sum Distribution Test

Sometimes fixes cannot be completed with proactive measures by the account owner. However, the correction occurs due to subsequent life events. One such fix can happen after a person fails the lump sum distribution test as it applies to net unrealized appreciation (NUA). NUA is the increase in the value of the employer stock from the time it was acquired in the plan to the date of the distribution to the plan participant.

With the NUA tax break, a participant in a company plan can withdraw their stock from the plan and pay regular (ordinary) income tax on it but only on the original cost and not on the market value (i.e., what the shares are worth on the date of the distribution). The difference or appreciation is NUA.

Example: Harry can elect to defer the tax on the NUA of the company stock distributed from his 401(k) until he sells that stock. When Harry does sell it, he will only pay tax at the long-term capital gains rate.

To qualify for the tax deferral on NUA, Harry's distribution must be a lump sum, meaning all the assets in all like-plan accounts must be distributed. The distribution must occur in one calendar year, and the plan balance must be zero by the end of that year. Most importantly, the lump sum distribution can only occur after one of these four triggering events:

1. Reaching age 59½;
2. Separation from service;
3. Disability; *or*
4. Death.

What if Harry reaches age 59½ and attempts to complete an NUA transaction but fails to completely empty his account? The NUA benefit is lost, because Harry failed the lump sum distribution test. He can't fix this specific transaction, but Harry can