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2015 resolution: Avoid 60-day rollovers

Strict new rules on IRA fund transfers are now in effect, and breaking them can be costly

By Ed Slott | *January 4, 2015 - 12:01 am EST*

As of Jan. 1, owners of individual retirement accounts can do only one 60-day rollover a year, for all their IRAs. The rule no longer applies separately to each IRA. In this case, IRAs include traditional and Roth IRAs, as well as SEP and Simple IRAs.

The one-year period is not a calendar year; it's 365 days or 12 months. If a second 60-day rollover takes place within the one-year period, the distribution will be taxable and subject to a 10% early-withdrawal penalty if the client is under 591/2.

Should clients attempt a second rollover, the problem cannot be fixed. The IRS does not have the authority to help correct the situation. This could end an IRA, for example, if clients were moving their entire IRA balance to a new custodian or a new adviser.

It can get worse. If clients do a second 60-day rollover, it's now not only taxable but an excess IRA contribution subject to a 6% penalty each year the ineligible rollover funds remain in the account.

As a review, there are two ways to move money from one IRA to another: directly and indirectly. Always move IRA funds directly if you can.

With a direct transfer — also called a trustee-to-trustee transfer — the funds move directly from one IRA to another without the client's touching the money. Direct transfers can be done as often as a client wishes, without having to worry about the one-a-year IRA rollover rule.

With the indirect transfer — also called a 60-day rollover — clients receive a check from their IRA made out to them personally. They have 60 days from the receipt date to redeposit those funds into another IRA, or even back to the same IRA.

Advisers should avoid indirect, 60-day rollovers like the plague.

This issue surfaced as a result of the Bobrow tax court case about a year ago (Alvan L. Bobrow, et ux. v. Commissioner, TC Memo 2014-21, Docket No. 7022-11, Jan. 28, 2014). Before then, the published tax rules (IRS Publication 590) allowed the once-per-year rule to be applied separately to each IRA.

In the Bobrow case, the court held that Mr. Bobrow, a tax lawyer, was taking advantage of the 60-day rule for each IRA. He had done a series of rollovers from separate IRAs and had use of his IRA funds for almost six months.

The court essentially said, “No more of this nonsense.” Mr. Bobrow lost his case, and that changed the interpretation of the once-per-year rule for everyone.

The court said that the rule applies to all IRAs, not to each one separately. The IRS agreed and changed the rules in March with IRS announcement 2014-15.

The IRS provided relief for 2014 rollovers that would have been legal under the separate-account treatment but are not anymore.

In addition, the IRS confirmed that if the custodian of the individual retirement account makes a check payable to the receiving custodian rather than to the client personally, that check will qualify as a trustee-to-trustee transfer. Therefore, it will not be subject to the once-per-year rollover rule.

The rule also does not apply to rollovers from retirement plans such as 401(k)s or 403(b)s to IRAs or from IRAs back to plans. Rollovers from a traditional IRA to a Roth IRAs (also know as a Roth conversion) are also exempt from the once-per-year rollover rule.

Advisers need to be up to speed on the new rule interpretation and let all clients know about it. Be careful taking in new IRA rollovers as a 60-day rollover.

If you do that, you'll have to ask if clients did any 60-day rollovers of their traditional or Roth IRA funds within the past year. If they did, they cannot do another within the period.

It's best for advisers to steer clear of 60-day rollovers. Instead, insist on direct transfers, both when taking on new clients with IRA rollovers or helping existing clients with them.

Ed Slott, a certified public accountant, created the IRA Leadership Program and Ed Slott's Elite IRA Advisor Group. He can be reached at irahelp.com.