WATCH OUT FOR THE ONCE-PER-YEAR ROLLOVER RULE

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Why is it so important to know how the once-per-year rollover rule works? Well, that is because trouble with the once-per year rule is the kind of trouble no one wants! An IRA owner who violates this rule is looking at some serious tax consequences.

One Rollover a Year for an IRA owner

If an IRA owner for whatever reason elects not to do a direct transfer but instead chooses to move her money by a rollover, then there will usually no escaping the once-per-year rollover rule. The rule says that an IRA owner cannot roll over an IRA distribution that was received within 12 months of a prior IRA distribution that was rolled over.

Traditional and Roth IRAs are combined for purposes of the once-per-year rule. A distribution and subsequent rollover between your Roth IRAs will prevent another rollover of a traditional IRA received within one year from receipt of the Roth. The bottom line is that only one IRA-to-IRA (or Roth IRA-to-Roth IRA) 60-day rollover may be done if the distributions are received within 12 months of each other.

Fatal Error

A mistake with the once-per-year rollover rule can result in the loss of your retirement savings. It is a fatal error with no remedy.

If an IRA owner takes a distribution with the intent of rolling it over and discovers that she is ineligible to roll over the funds due to the rule, that distribution will be taxable to her. She will no longer have an IRA and will likely have a tax bill instead. The distribution will also be subject to the 10% early distribution penalty if the IRA owner is under age 59 ½. If she goes ahead and deposits the funds anyway, she will have an excess IRA contribution complete with all the penalties and headaches that go with it. What about the IRS? Well, the IRS will not be able to grant relief. This is because by law the IRS has no authority to waive this rule. The self-certification procedures which allow for relief when the 60-day rollover deadline is missed do not apply to violations of the once-per-year rollover rule. A private letter ruling (PLR) request won't work either.

Direct Transfers Are the Way to Go

Why chance it? A good place to start is by avoiding 60-day day rollovers whenever possible. If there is no 60-day rollover, then there is no once-per year rollover rule to worry about. How then can you move your retirement funds? The best advice is to directly transfer the funds from one retirement account to another instead of taking a distribution payable to yourself and then rolling it over to another retirement account. You can do as many transfers between IRAs annually as you want. There are no limits to worry about.