

# IRA TRANSACTIONS THAT CAN BE MISSED

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Not every IRA transaction is easily identifiable. Some require a little legwork to reveal or report what occurred. Some transactions are not even labeled on official IRS tax forms and can go undetected. Here are three items that taxpayers and tax professionals alike can easily miss.

**1. Qualified Charitable Distributions (QCDs) NOT Reported on 1099-R.** IRA custodians will not separately report a QCD. There is no code or box on the 1099-R to identify a QCD. It is up to the taxpayer to let the IRS know about the donation by including the information on the tax return. Since there is no 1099-R reporting code, tax preparers/CPAs must be alerted. QCDs can easily be missed on a tax return, resulting in an erroneous taxable IRA distribution.

The lack of a QCD code on the 1099-R is intentional. This is not an oversight by the IRS, and is most likely a welcome relief for custodians. Why? Because an IRA custodian does not have first-hand knowledge of whether a particular distribution meets all the QCD conditions. Is it a qualifying charity? Did the person already max out the \$100K QCD limit from another IRA at another firm? Custodians do not want to police any of these details.

**2. Tracking Roth IRA Contributions and Roth Conversions.** IRS Form 5498 contains a bevy of information, including a definitive date for every Roth contribution and conversion.

Box 3 – Roth conversions. Until a person is age 59 ½, every Roth IRA conversion will carry its own 5-year clock to determine whether distributions of the converted amounts are subject to the 10% early distribution penalty. It is all recorded on the annual Form 5498. A Roth conversion is essentially time-stamped January 1 for the

year listed on the form. Add five years and a Roth IRA owner will know exactly when those Roth conversion dollars are available penalty-free.

Box 10 – Roth IRA contributions. Roth contributions are also time-stamped on a 5498. Technically, there is no place on a 1040 to report a Roth contribution. So how does the IRS know when a person opened his first Roth IRA and set the “5-year forever clock” in motion for distributions of tax-free earnings? See Form 5498.

**3. Forgetting to File 8606 to Claim Basis (After-Tax Contributions).** How do you tell the IRS that an IRA distribution or Roth conversion is not taxable? After all, the IRS will treat it as ordinary income unless there is evidence that it should not be taxed. The answer is IRS Form 8606. IRA custodians do NOT keep track of after-tax contributions – even if you tell them that the funds are after-tax or keep the after-tax dollars in a separate IRA. Custodians have no way of knowing what a person claims on his tax return, so they have no way of knowing if a deduction for an IRA contribution was taken or not.

Any time an after-tax contribution is made to an IRA, IRS Form 8606 must be filed. This is essentially the client waving a flag and declaring, “I have after-tax funds in my IRA!” Without this form, the IRS will assume that any funds distributed from the IRA (or converted to a Roth IRA) are taxable.

Be careful not to overlook any of these all-important items!

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