

Rollover Distributions to Qualified Plans Should Not Take Basis

[Section 408\(d\)\(3\)\(H\)\(ii\)\(II\)](#) provides that if there is a nontaxable rollover from a traditional IRA to a qualified plan (such as a 401(k)), the distribution does not take with it any basis in the traditional IRA.

Natalie B. Choate, in her excellent treatise [Life and Death Planning for Retirement Benefits](#) (8th Edition 2019), discusses this issue on pages 152 and 153. On page 153, she states that IRA distributions that are rolled over into other IRAs or qualified plans do not count as distributions for purposes of the Pro-Rata Rule. Thus, they do not attract any of the basis created by previous (or future) nondeductible traditional IRA contributions.

Ms. Choate's treatise cites to Notice 87-16, which also provides that nontaxable rollovers to other retirement accounts factor into neither the numerator nor the denominator of the Pro-Rata Rule.

Vorris J. Blankenship discussed this issue in the text accompanying footnotes 90 to 93 in his 2006 article [Determining Taxpayer Investment in Retirement Plans and IRAs](#). Mr. Blankenship observes that under Section 408(d)(3)(A)(ii), it is not permissible to rollover IRA basis into a qualified plan (only amounts that would be taxable upon distribution can be moved from a traditional IRA to a qualified plan).

Additional Notes

It is important to note that the Pro-Rata Rule functions at year-end on all distributions (unless otherwise exempted, such as the IRA to 401(k) rollover). See Section 408(d)(2). This is logical, otherwise each distribution would need to be separately reported and computed on its own Form 8606, and each distribution would remove a different proportion of the basis. This would make compliance a nightmare. Fortunately, Section 408(d)(2) simplifies things with one year-end calculation, and that is reflected on the Form 8606.

Inherited IRAs (non spousal) with basis are tracked entirely separately from the beneficiary's own Pro-Rata Rule calculation applicable to the IRAs the owner owns as the original owner. See Choate, page 151.