Estate Planning For IRAs

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Primary Estate Planning Goals (Financial)

1) Transfer assets as efficiently as possible!

2) Make sure that assets get to the right people!

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The "I" in IRA

- IRAs present unique challenges because they are always in the owner's estate
- IRAs/inherited IRAs cannot be "moved" into trusts
- Exceptions
  - PLR 201116005 (SNT)
  - PLR 200620025 (SNT)
  - PLR 200826008 (Minor)

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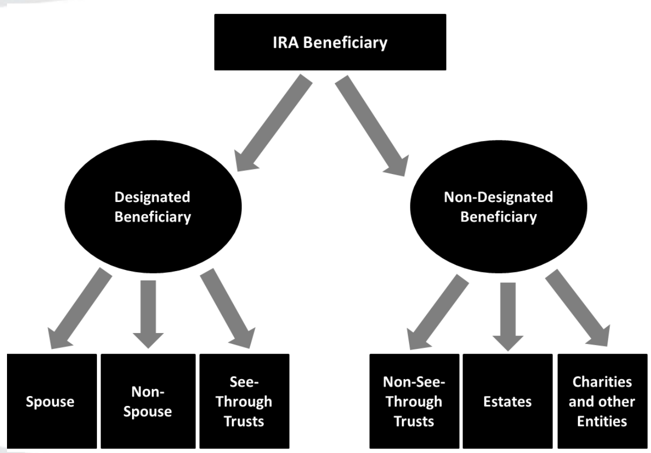
The IRA Beneficiary "Family Tree"



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Key Post-Death Deadlines

- September 30th "Cash-out" date
  - Utilize to eliminate unwanted beneficiaries
- December 31st "Account Splitting" deadline
  - Utilize to allow multiple beneficiaries to use their own life expectancies to calculate RMDs
- Disclaimer deadline
  - Generally 9 months after date of death

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Year-of-Death RMD and Disclaimer Concerns

- Year-of-death RMD must be taken by beneficiary!
- Taking RMD does not preclude disclaimer of remaining funds
- Revenue ruling 2005-36

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Post-Death Disclaimers Requires Pre-Death Planning

- Disclaimers only work if the "path" has been property established (before death!)
- Use contingent beneficiaries
  - Can often go "deeper" with customized beneficiary forms
- Per stirpes vs. per capita vs. alternate methods

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Non-Designated Beneficiary

- Estates, charities, businesses, pets(!), non-see-through trusts
- Death of owner prior to RBD
  - 5-year rule
- Death of owner on/after RBD
  - Remaining single life expectancy of decedent

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Charity As Beneficiary

- Consider splitting out in a separate account during lifetime
- Often the "best" asset to leave a charity
- Also often the best source of near-death charitable giving for those 70 ½ or older
  - QCD
  - Limited to $100,000 per year

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Designated Beneficiaries

- Named on the beneficiary form
  - Living persons
  - Qualifying see-through trusts
- Inherit via default beneficiary language
- Death of owner prior to RBD
  - Beneficiary can "stretch" distributions over single life expectancy
  - Beneficiary can opt into the 5-year rule
- Death of owner on/after RBD
  - Beneficiary can stretch distribution over longer of own single life expectancy or single life expectancy of decedent

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Impact Of The SECURE Act

- "Stretch" eliminated for designated beneficiaries and replaced with a "10-Year Rule" EXCEPT in situations where the beneficiary is:
  - The surviving spouse
  - A child under the age of majority
  - Disabled
  - Chronically ill
  - Not more than 10 years younger than the IRA owner

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Planning Impact of the SECURE Act

- Reevaluate beneficiaries
- Build in flexibility to the plan
- Accelerate Roth IRA conversions (for legacy planning)
- Permanent life insurance becomes more valuable
- Use charitable trusts to recreate the stretch IRA

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SPOUSAL BENEFICIARY OPTIONS*

1) Remain as a beneficiary of the inherited account (with special rules)
2) Complete a spousal rollover
3) Elect to treat the deceased spouse's account as their own

* Spouse must be sole beneficiary

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REMAINING A BENEFICIARY

- No 10% penalty on pre-59 ½ distributions
- Properly titled inherited IRA is established
- Funds must be moved directly
- No RMDs until deceased spouse would have been 70 ½
  - Spouse beneficiaries subject to RMDs can recalculate their life expectancy (but still use the Single Life Expectancy Table)
- Special rule for successor beneficiaries

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SPOUSAL ROLLOVER

- Often makes sense if surviving spouse is ≥59 ½
- Irrevocable election
- Treated as though money was always in the surviving spouse's IRA
- No deadline to complete

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THE "99% RULE"

"If the surviving spouse is under 59 ½, then setting up an inherited IRA is almost always the correct option. Once the spouse turns 59 ½, a spousal rollover can be completed."

"If the surviving spouse is 59 ½ or older, a spousal rollover is almost always the right move."

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Potential Exceptions to the "99% Rule"

- Scenario #1
  - Much younger spouse (<11 years younger)
  - Deceased spouse would already be 70 ½ or older
  - Surviving spouse does not anticipate needing inherited IRA money until they are at least 59 ½
- Scenario #2
  - Older spouse
  - Younger spouse would not yet be 70 ½
  - Spouse beneficiary doesn't need/want to take distributions

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Trusts As IRA Beneficiaries

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Reasons to Name a Trust as an IRA Beneficiary

- Control
  - Minor beneficiary
  - Disabled beneficiary
  - Unsophisticated beneficiary
  - Concerns over future marriages and/or disposition of assets
  - To guarantee "the stretch" IRA is used
  - To keep money away from creditors
  - To keep money away from a beneficiary's spouse/ex-spouse
  - To mimic "the stretch" via a charitable trust
  - For other charitable trust planning

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Reasons NOT To Name a Trust As Beneficiary

- To save money on income taxes
- To save money on estate taxes
- "Because my attorney said so"
- Complexity
- Cost

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See-Through Trusts

- Also known as look-through trusts
- Allow trust to "stretch" distributions over oldest applicable trust beneficiary's life
- No separate account treatment for trust beneficiaries
  - One beneficiary named on beneficiary form = one life expectancy
  - Can use and NAME subtrusts on beneficiary form to use multiple life expectancies
- Must meet certain requirements

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Regulation 1.401(a)(9)-4, A-5

- Valid under state law
- Irrevocable at death
- Trust beneficiaries are identifiable
- Proper documentation is provided to the custodian by October 31st of the year following the year of death

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Life Cycle Of An IRA Trust

- Owner determines there is a post-death control issue that requires the use of a trust
- Trust is drafted by a qualified estate planning attorney (can be a testamentary trust)
- The trust is named as the beneficiary on the beneficiary form
  - John Doe IRA trust
  - John Doe IRA trust established under Article X Section X of John Doe Last Will and Testament

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Life Cycle Of An IRA Trust

- IRA Owner Dies
- Properly titled inherited IRA is established FBO the trust
  - John Smith (deceased January 3, 2019) IRA fbo John Smith Trust
- Distributions go from the inherited IRA to the trust
- Distributions go from the trust to the trust beneficiaries per the terms of the trust

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Two Types of See-Through Trusts

- Conduit Trusts
- Discretionary Trusts
  – Also known as accumulation trusts

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Conduit Trusts

- No less than the RMD *required* to be distributed to trust beneficiaries each year
- Trust beneficiaries pay income tax on RMDs at their own personal rates
- Only income beneficiaries of the trust are looked at to consider oldest age for RMDs

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Conduit Trusts

- Advantages of conduit trusts include:
  - Potentially more tax efficient than discretionary trusts
  - Any remainder beneficiary can be used without ruining the stretch IRA
- Disadvantages of conduit trusts include:
  - Less post-death control

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Discretionary Trusts

- RMDs from the inherited IRA may be accumulated in the trust
  - RMDs may also be distributed out of the trust, depending on the language of the trust
- Distributions from an inherited IRA not passed along to trust beneficiaries within the same year are taxed at trust tax rates
  - Consider using the 65-day rule
- All current and potential beneficiaries of the trust are looked at to consider oldest age for RMDs
  - Current beneficiaries
  - Remaindermen

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Discretionary Trusts

- PLR 200228025 v. 201320021
  - Both PLRs involve discretionary trusts
  - Both PLRs address the issue of contingent beneficiaries
  - PLR 200228025 left assets to 2 grandchildren, but if both died prior to 30, older contingent beneficiaries would receive funds
  - PLR 201320021 left assets to trust for children's benefit, did not name contingent beneficiaries
    - Is staying silent the better option? Perhaps…

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Discretionary Trusts

- Advantages of discretionary trusts include:
  - Greater control over trust assets
  - Easier to keep assets away from:
    - Creditors
    - Ex-spouses
- Disadvantages of discretionary trusts include:
  - Greater possibility for conflict between trustee and trust beneficiaries
  - Distributions may be taxed at compressed trust tax brackets
  - Non-designated remaindermen beneficiaries will cause stretch to be blown

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Discretionary Trusts

- Discretionary Trust Idea:
  - Consider Roth conversions during owner's lifetime
    - Inherited IRAs cannot be converted to inherited Roth IRAs
    - Inherited plans (e.g. inherited 401(k)) can be converted to inherited Roth IRAs
  - Inherited Roth IRAs can generally avoid the tax issues that are present with traditional IRAs

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Trust Review: What To Look For

1) Is there language that calls for debts and expenses of the estate to be paid from trust assets
2) What is trust income?
3) How flexible is the trust?

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"Debts and Expenses of the Estate" Language

- Estate is treated as a beneficiary of IRA
  - An estate is not a designated beneficiary
    - Stretch IRA can be blown
  - Creditor protection of the inherited IRA may be compromised
- To remove an estate as a trust beneficiary, utilize the September 30th cash-out date
- "Shall" vs. "may" vs. staying silent
- Trust expenses are ok

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What Is Trust Income?

- Uniform Principle and Income Act (UPAIA)
  - Adopted by roughly 45 states
  - Defines 10% of RMD as income, 90% principal
- Income using the Unitrust concept
  - Must be allowed by state law
  - Federal regulations allow for unitrust rate to be set between 3% and 5%
- Uniform Fiduciary Income Act
  - Newly established
- Check to see if trust uses the term "income" or "RMDs"
- Consider defining "income" within the trust

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Is There Built-In Flexibility For the Trust?

- An IRA trust may last many decades
- Laws may change substantially during that time
- Consider provisions allowing change of situs
- Consider allowing the trust to be terminated if no longer necessary
  - Beneficiary's issues are resolved
  - Trust assets no longer justify the use of a trust

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Everyone's "Favorite" Game Show

WHO GETS THE MONEY?

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Who Gets The Money?

- Kennedy v. Plan Administrator for DuPont Savings and Investment Plan, U.S. Supreme Court, No. 07-636, January 26, 2009
- Cajun Industries, LLC vs. Robert Kidder, et al. United States District Court; Middle District of Louisiana, No. 09-267-BAJ-SCR – April 26, 2011
- Greenebaum Doll & McDonald PLLC v. Sandler, U.S. Court of Appeals for 6th Circuit, No. 06-6496, December 3, 2007

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IRAs: The Beneficiary Form Controls Disposition

- Charles Schwab & Company v. Chandler, No. 07-15261, D.C. No. CV-06-00119-FJM (CA 9 - 1/22/2010)
- "The Pension Pickle," New York Post, January 31, 2005

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Other "Who Gets It?" Complications

- Community property laws
- Auto-elimination of ex-spouses via
  - State law
  - Contract
- Different definitions of "children"
- Revoking a will that contains a testamentary trust

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