PLANNING FOR OWNERSHIP AND INHERITANCE OF PENSION AND IRA ACCOUNTS AND BENEFITS IN TRUST AFTER THE SECURE ACT

The Estate Planner's IRA/Pension Planning Guide

SECURE Act Checklist Included Inside!

WITH FULL COVERAGE OF THE 2019 SECURE ACT, THE 2020 CARES ACT, AND PROPOSED REGULATIONS ON PENSION AND IRA ACCOUNTS

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PREFACE

By Jerome M. Hesch

When examining books designed to offer a comprehensive discussion of a particular topic, the casual reader can be overwhelmed by the rules and the technical details.

Although the Gassman book on IRA planning includes comprehensive coverage of the topic, it does something not normally found in definitive discussions. The first thing I noticed is that for each subject, the book provides a brief analysis of the reasons for the rules governing the subject. With a preliminary understanding of the principles a rule was designed to accomplish, the reader can apply the rule to a client matter without the need to reference the exact language in the rule that needs to be addressed. One can later verify their initial conclusion by examining the statute, regulation, ruling or the reference book they are using.

This leads me to my second observation. When there is an understanding of reasons, it allows the advisor to communicate the analysis more effectively to a prospective client without becoming overly technical. To further develop the ability to communicate highly technical tax rules in an understandable manner, the book contains frequent numerical examples to illustrate the application of the rules. Using illustrative examples allows one to communicate a structure without having to resort solely to the use of complicated descriptions filled with technical terms.

My final observation is that the book evaluates the different planning techniques so that one can more effectively evaluate the one most suitable for each client's situation. This has become even more important with the change in the income tax deferral for inherited IRAs.

The book provides a resource for those who are not expert in the rules underlying IRAs to elicit a more comprehensive understanding, thereby more effectively serving their clients.

PURPOSES THAT CAN BE SERVED BY THIS HANDBOOK

1. Understanding the rollover, aggregation/non-aggregation, creditor protection, borrowing, and Required Minimum Distribution rules as they apply to Plan Participants and their beneficiaries.

2. Understanding the different methods of calculating Required Minimum Distributions and when each of them applies.

3. Understanding what post-death decisions can be made and what flexibilities can be programmed into an estate and trust plan, so that the best-possible decisions can be made during the nine months after the death of the IRA/Plan Participant.

4. Understanding how to determine the best way to integrate Roth and traditional IRA and plan-distribution planning with QTIP (qualified terminable interest property) marital deduction trusts, generation skipping trusts, and non-generation skipping trusts.

5. Understanding the differences in the payout rules that apply based upon whether the deceased IRA owner/plan beneficiary was receiving Required Minimum Distributions because of having reached his or her Required Beginning Date.

6. Understanding annuitized IRA contracts, qualified longevity annuity contracts (QLACs), and beneficiary designation planning under non-qualified variable annuity contracts.

7. Understanding the SECURE Act, which was enacted December 20, 2019, and is covered throughout this Book and in great detail in Chapter 7.

8. Understanding the Proposed Treasury Regulations that were released on February 24, 2022, which are covered throughout the Book and in detail in Chapter 8.

INTRODUCTION

"If you are not confused, you are not paying attention."

Tom Peters, author of *Thriving on Chaos*, *A Passion for Excellence*, *The Pursuit of WOW!*, and others

Under the 80/20 Rule, 80% of any given project can be completed with 20% of the effort by proper organization and implementation.

Oftentimes 80% of the project is all that a Plan Participant needs to have completed, if he or she leaves the other 20% for customization when circumstances arise.

This is particularly important in the world of planning for IRA/Plan account disposition, where the details associated with each alternate strategy and situation can exceed even the brightest and most conscientious planners' ability to memorize.

The objective of this Book is to provide both novice and experienced planners a concise and complete, yet easy-to-use, guide to the following:

1. Understanding the primary rules, planning techniques, and traps for the unwary, and how the landscape has changed as a result of the SECURE Act becoming law effective January 1, 2020;

2. Providing charts and explanatory tools that can be used to explain and illustrate the rules; and

3. Finding further sources of explanation and guidance from other literature, including IRS regulations and rulings, books, articles, and reference materials.

Any conscientious estate planner can readily attest to the confusing array of rules, exceptions, and misconceptions that presently exist in the area of planning with IRA/Plan assets, and to the wide-reaching and complicated effect that the SECURE Act has on this area.

The charts on the following pages provide an organized description and ready reference text for both novice and experienced estate planners who wish to understand how these rules work.

We have worked hard to fit this project onto as few pages as possible without losing sight of important rules or planning opportunities. The fact that Natalie Choate's book, *Life and Death Planning for Retirement Benefits*, which is considered by most to be the leading guide in this area, is 500 pages long is a perfect example of how much more detail may need to be considered by conscientious planners.

We wish to thank Edwin Morrow, John N. Beck, and Stetson University College of Law student Peter Farrell for their contributions to this Book. We also thank a number of qualified IRA/Plan tax law experts who have blazed the extremely difficult and detailed trails that we have followed, most notably including Natalie Choate, Marcia Chadwick Holt, and Steve Trytten.

Table of Contents

Table of Charts

Appendix

Table of Authorities

Cases

Statutes

Other Authorities

U.S. Code Sections that are not in the Internal Revenue Code

Regulations

Internal Revenue Code (Title 26 of the U.S. Code)

Private Letter Rulings; Revenue Rulings; Revenue Procedure; IRS Chief Counsel Advice; and Other IRS Notices

CARES Act

CHAPTER 1 – INTRODUCTORY KNOWLEDGE

This Chapter covers basic information about IRA/Plan contribution and withdrawal rules. Most practitioners experienced in this area will skip this Chapter and go on to the more technical explanations that follow in subsequent chapters, but many will use this Chapter for refreshing or supplementing their knowledge of the basic rules that apply. There are many specialized terms and definitions that need to be reviewed in order to understand the context and technical rules in this Chapter. Accordingly, any capitalized terms that are not defined in this Chapter are defined in Chapter 2.

There are many stages of IRA/Plan distribution planning, and many types of interactive knowledge needed. This Chapter focuses on the basics: how individuals can establish and fund an IRA, selecting the most beneficial type of IRA for their situation, and how to make the best use of IRAs. Discussion will include regular IRAs, Coverdell Education Savings Accounts, Roth IRAs, rollovers, creditor protection, transferring IRAs, and age limitations.

IRA Basics

An Individual Retirement Account or "IRA" is a type of account that allows employees and self-employed individuals, who are not active participants in an employer-maintained retirement plan, to set aside and deduct up to $6,000 (or $7,000 in certain circumstances) for contributions. The IRA itself is essentially a trust account or custodial arrangement that holds permitted investments with a custodian that is typically a bank, savings and loan association, credit union, trust company, or other appropriately registered organization.

The 2019, 2020, 2021, and 2022 IRA contribution rules are as follows:

Basic Contribution limit is the lesser of:

a. $6,000 (but $7,000 if over the age of 50); or

b. Taxable compensation for the year, if the individual's compensation is less than the $6,000 ($7,000 if over the age of 50) dollar limit; and

Reduced by the amount of Roth contributions made in the applicable calendar year.

However, it is important to note that there are a number of special rules applicable to the IRA contribution limit. For example, it is not applicable to Rollover Contributions or qualified reservist repayments.[1] Furthermore, if the Plan Participant (or his or her spouse) is covered by a qualified

[1] Rollover Contributions are pre-retirement payments an individual receives from either a retirement plan or an IRA that may be "rolled over" if the payment is deposited into either another retirement plan or an IRA within 60 days. *Rollovers of Retirement Plan and IRA Distributions*, I.R.S., https://www.irs.gov/retirement-plans/plan-participant-employee/rollovers-of-retirement-plan-and-ira-distributions (last visited Jul. 25, 2022). It is possible for the individual's financial institution to directly transfer the payment. *Id*.

plan at work and the Plan Participant's (and/or his or her spouse's) income exceeds certain thresholds, there are additional limitations. Specifically, participation in another retirement plan through a business or employer does not foreclose the ability to contribute to either a traditional IRA or Roth IRA, but participation in a work retirement plan by an individual or his or her spouse may limit the ability to deduct traditional IRA contributions.

Nevertheless, most affluent Americans who participate in IRA/Plans will still fund an IRA, but on a non-deductible basis. Further, even if an individual's spouse limits his or her ability to deduct all of his or her traditional IRA contributions, contributions can still be made on a non-deductible basis. Many workers who cannot contribute to their own IRA because they have higher income and participate in a qualified plan may still be able to make deductible contributions to a non-working spouse's IRA.

Contribution limits for a person who is covered by a retirement plan at work (and his or her spouse) are based upon the individual's filing status and the individual's modified "adjusted gross income" (AGI).

Modified adjusted gross income (MAGI) is calculated by adding back the following deductions from the Plan Participant's AGI:[2]

1. One-half of payroll taxes deducted by a self-employed individual;
2. Student loan interest;
3. Tuition and fees deduction;
4. Qualified tuition expenses;
5. Passive income or loss;
6. Rental losses;
7. IRA contributions and taxable Social Security payments;
8. Exclusion for income from U.S. savings bonds; and
9. Exclusion for adoption expenses (under §137).

Limits on Deductibility of Traditional IRA Contribution Based on the Plan Participant's Filing Status[3]

An individual covered by a retirement plan at work who files federal income tax returns as single or the head of household with a MAGI of $68,000 or less will retain a full deduction of up to the

[2] The IRS provides a worksheet (Exhibit 2.2: Modified Adjusted Gross Income Computation) at the following address that can be used to calculate MAGI: https://www.irs.gov/pub/irs-mssp/pal.pdf.

[3] Individuals filing single or head of household with income greater than the IRA contribution limit but less than the Roth IRA contribution limit should consider contributing amounts to a Roth IRA.

amount of his or her respective contribution limit.[4] If the individual covered by a retirement plan at work has a MAGI between $68,000.01 and $78,000, he or she will receive a partial deduction on a pro-rata basis. If the individual covered by a retirement plan at work has a MAGI of greater than $78,000, he or she will not receive a deduction for funding an IRA.

An individual covered by a retirement plan at work who files jointly or is a qualifying widow(er) with a MAGI of $109,000 or less will receive a full deduction of up to the amount of his or her respective contribution limit.[5] With a MAGI between $109,000.01 and $129,000, he or she will receive a partial deduction, and an individual with a MAGI greater than $129,000 will not receive a deduction.

Where the individual is married but filing separately with a MAGI of less than $10,000, he or she will receive a partial deduction.[6] If he or she is filing with a MAGI greater than $10,000, he or she will not receive a deduction. If a married couple is filing separately but did not live together at any time during the year, then the IRA deduction is determined based on a "single" filing status.[7]

These contribution rules apply only if the Plan Participant is covered by a Qualified Retirement Plan at work. If neither the IRA contributor nor his or her spouse is covered by a Qualified Retirement Plan at work, then there are no income limitations and the Plan Participant can contribute up to the contribution limit of $6,000 (or $7,000 if the Plan Participant is over the age of 50).

An individual who is married and filing jointly whose spouse is covered by a retirement plan at work and has MAGI of less than $204,000 will receive a full deduction. With a MAGI between $204,000.01 and $214,000, he or she will receive a partial deduction, and an individual with a MAGI greater than $214,000 will not receive a deduction.

The IRS website has a very helpful chart regarding these contribution limits, which can be found at the following link:

https://www.irs.gov/retirement-plans/plan-participant-employee/2022-ira-contribution-and-deduction-limits-effect-of-modified-agi-on-deductible-contributions-if-you-are-covered-by-a-retirement-plan-at-work

In order to deduct contributions for the applicable tax year, contributions must be made prior to the due date for federal income tax returns (without regard to extensions), which for the vast

[4] Under Section 72, basis is normally allocated equally between each of the annual payments that are scheduled to be made until the original life expectancy of the beneficiary has been reached, with any payment received from then on being treated as 100% ordinary income.

[5] *2022 IRA Contribution and Deduction Limits Effect of Modified AGI on Deductible Contributions If You Are Covered by a Retirement Plan at Work*, I.R.S. (Nov. 5, 2021), https://www.irs.gov/retirement-plans/plan-participant-employee/2022-ira-contribution-and-deduction-limits-effect-of-modified-agi-on-deductible-contributions-if-you-are-covered-by-a-retirement-plan-at-work.

[6] *Id*.

[7] *Id*.

majority of taxpayers is April 15th of the following tax year.[8] A contribution made prior to the filing of the tax return due date is eligible to be treated as if it were made in the previous year. The contribution date cannot be extended, even if the taxpayer extends his or her personal income tax return (Form 1040) by filing a Form 4868.

Coverdell Education Savings Accounts

A Coverdell Education Savings Account (Coverdell ESA), formerly known as the Educational IRA, is set up to pay for the education expenses of a Designated Beneficiary. If the Plan Participant's MAGI is less than $110,000 (or less than $220,000 for a joint return), he or she may be able to establish a Coverdell ESA. For most Plan Participants, MAGI is the adjusted gross income as determined on his or her federal income tax return.[9]

Coverdell ESAs can be a great way for grandparents to set money aside for grandchildren to cover future higher elementary and secondary education. There is no limit on the number of separate Coverdell ESAs that can be established for a Designated Beneficiary, but the total contributions for each Designated Beneficiary cannot exceed $2,000 per year, regardless of the number of accounts established. If an individual is above the income limitation or wishes to contribute additional amounts, then contributions can be made into a 529 Plan. Coverdell ESAs allow for tax-free growth and tax-free withdrawals to pay for permitted educational expenses, similar to the 529 Plan rules.

Quick Facts on Coverdell ESAs

1. Contributions are limited to $2,000 per year, per beneficiary, in the aggregate. The limitation is on the total amount that the child can receive per year, not on the amount contributed by each person. Therefore, one individual can contribute to as many Coverdell ESAs as he or she wants to in a given year so long as the total amounts contributed to all accounts for the benefit of a particular beneficiary do not exceed $2,000. If multiple parties contribute to a Coverdell ESA for one beneficiary, the total contributions in the aggregate cannot exceed $2,000 in a given year for that beneficiary.

2. The balance must be disbursed for qualified education expenses before the beneficiary reaches age 30 to avoid penalties and taxes.

3. Coverdell ESAs can be used for primary and secondary education expenses and are not limited to college education expenses. 529 Plans previously could be used only for college education expenses, but the 2017 Tax Cuts and Jobs Act changed this to allow 529 Plans to be used for up to $10,000 per calendar year for kindergarten through 12th grade tuition payments, making Coverdell ESAs less attractive.

[8] The April 15th deadline was moved to July 15th for 2020 contributions that were to be reported on 2019 income tax returns under the CARES Act. This is consistent with the income tax filing deadline for 2019 federal income tax returns which were postponed to July 15, 2020, by the IRS as a result of the COVID-19 pandemic.

[9] See an excellent article written by Lawrence Katzenstein at LISI Charitable Planning Newsletter #292 (February 10, 2020) at http://www.leimbergservices.com.

4. It is possible for a child to contribute to his or her own Coverdell ESA. If the contributor's MAGI is greater than the limitation, then a gift of $2,000 can be made to the child and the child can contribute the money to the Coverdell ESA, assuming the child's MAGI is below the income-limitation amount.

5. Organizations such as corporations and trusts can also contribute, and there is no requirement for the organization's income to be below a certain level.

6. No contribution can be made after a beneficiary reaches age 18, unless the beneficiary is a special-needs beneficiary.

Roth IRA

A Roth IRA is a special retirement account that allows the holder to withdraw monies tax-free under most circumstances. The benefit of a Roth IRA is that the holder can access the contributions in the account at any time tax-free and penalty-free. The Roth IRA is also beneficial to young workers that do not have a substantial income but will likely have a greater income in the future, because taxes will not be imposed upon the withdrawal of the Roth IRA monies. In addition, a Roth IRA can be beneficial if an individual believes that his or her tax rate may be higher during retirement than the current rate at which he or she is being taxed.

However, not everyone meets the standards to contribute to a Roth IRA because there is a cap on the allowable income level. To qualify as an individual, a Plan Participant must have a MAGI of less than $144,000 to contribute to a Roth IRA for the 2022 tax year. If the Plan Participant is married, he or she must have a MAGI of less than $214,000 to contribute.[10] In addition, to qualify to be able to contribute to a Roth IRA, the Plan Participant must have "earned income" for the year of the contribution. Earned income is money paid for work that he or she performed, including wages, salaries, tips, bonuses, commissions, self-employment income, and also taxable alimony and military differential pay.[11]

The basic Roth IRA contribution limit for 2019, 2020, 2021, and 2022 is the lesser of:

a. $6,000 ($7,000, if over the age of 50); or

b. Taxable compensation for the year

Reduced on a dollar-for-dollar basis by contributions to traditional IRAs (See "IRA Basics" above).

If a taxpayer contributes to both a Roth IRA and a Traditional IRA, contributions in the aggregate cannot exceed the $6,000 limitation ($7,000, if over age 50).

[10] *Retirement Topics - IRA Contribution Limits*, I.R.S. (July 20, 2022), https://www.irs.gov/retirement-plans/plan-participant-employee/retirement-topics-ira-contribution-limits.
[11] *Id.*

In order to determine contribution limits, an individual must determine his or her filing status and MAGI. The formula provided by the IRS for 2022 is as follows:

1. Start with the MAGI.

2. Subtract the following from the MAGI:

    a. $204,000 if filing a joint return or qualifying widow(er).

    b. $0 if married filing a separate return, and the Plan Participant lived with his or her spouse at any time during the year, or

    c. $129,000 for all other individuals.

3. Divide the result in paragraph (2) above by $15,000 (or $10,000 if filing a joint return, qualifying widow(er), or married filing a separate return and the Plan Participant lived with his or her spouse at any time during the year).

4. Multiply the maximum contribution limit (before reduction by this adjustment and before reduction for any contributions to traditional IRAs) by the result in Paragraph (3) above.

5. Subtract the result in Paragraph (4) above from the maximum contribution limit before this reduction.

6. The result is the reduced contribution limit.[12]

For example, if an individual filing a joint return had a MAGI of $215,000, then he or she would not be eligible to contribute to a Roth IRA.

An individual filing jointly with MAGI of $208,000 is eligible to contribute to a Roth IRA, but his or her contribution would be limited to $3,600 based on the above formula as calculated below:

Step 1 - $208,000
Step 2 - $208,000 - $204,000 = $4,000
Step 3 - $4,000 divided by $10,000 = 40%
Step 4 – 40% of $6,000 = $2,400
Step 5 - $6,000 - $2,400 = $3,600
Step 6 - $3,600

The contribution is limited to $3,600, and $2,400 could be contributed by an individual to a non-deductible IRA.[13] The nondeductible contribution must be reported to the IRS on Form 8606.

[12] *Amount of Roth IRA Contributions That You Can Make for 2018*, I.R.S., https://www.irs.gov/Retirement-Plans/Plan-Participant,-Employee/Amount-of-Roth-IRA-Contributions-That-You-Can-Make-for-2018 (last visited Jul. 19, 2018).

[13] IRS Publication 590-A.

If an individual filing a joint return had MAGI of $180,000, then he or she would be able to contribute the maximum amount of $6,000 (or $7,000 if the individual is over the age of 50).

Converting a Traditional IRA into a Roth IRA

When an individual chooses to convert some or all of a traditional IRA to a Roth IRA, income tax has to be paid on the amounts converted. The taxable amount that is converted is added to the Plan Participant's taxable income and his or her regular income rate is applied to his or her total income.

Converting to a Roth IRA can be an effective method for an investor to cut tax losses. For example, if a taxpayer knows that his income will be increasing in the next year, thus increasing his tax bracket, and he converts his traditional IRA to a Roth IRA, then the tax bracket will remain at the lower tax bracket, thus allowing the taxpayer to save some money. Having a Roth IRA can also be a benefit when the government announces a tax rate increase for the upcoming year.

Upon conversion from a traditional IRA to a Roth IRA, the IRA account balance is subject to income taxes, except to the extent of basis, and conversion does not always make good sense.[14]

In the past, to convert from a traditional IRA to a Roth IRA, the Plan Participant's income had to be below $100,000. The IRS rules have changed and eliminated this cap, and therefore even a high-income taxpayer can convert a traditional IRA to a Roth IRA. This allows taxpayers who would otherwise be precluded from making contributions to a Roth IRA due to their income levels to make "back door" contributions to a Roth IRA by way of a conversion.

Having a Roth IRA guarantees that, under the present law, a Plan Participant will not owe income taxes on certain withdrawals. An investor who chooses to convert from a traditional IRA to a Roth IRA has until April 15th of the following year to make the conversion effective. For example, an individual converting his traditional IRA to a Roth IRA as of December 31, 2020 has until April 15, 2021 to effectuate the conversion by rolling over each traditional IRA into a Roth IRA.

Both traditional and Roth IRAs allow the owner to begin taking penalty-free, "qualified" distributions at age 59½; however, Roth IRAs require the first contribution to occur at least five years before qualified distributions begin.

If the Plan Participant has started taking substantially equal periodic payments from a traditional IRA, then he or she can still convert the amounts in the traditional IRA to a Roth IRA and continue the periodic payments. Tax will be owed upon the conversion, but future payments will be income tax free.

Plan Participants CANNOT convert amounts distributed in accordance with Required Minimum Distributions Rules into a Roth IRA and cannot convert an inherited traditional IRA into a Roth IRA.

[14] See LISI Employee Benefits & Retirement Planning Newsletter #549 (November 9, 2010) at http://www.leimbergservices.com, written by Alan S. Gassman, Kenneth J. Crotty and Christopher J. Denicolo, entitled One Good Reason Not To Do A Roth IRA Conversion.

Roth conversions are the subject of numerous well-written articles.[15]

We tend to agree with the sentiments of Ed Morrow, as expressed in Leimberg Information Services (LISI) Newsletter #192 (February 18, 2020) at http://www.leimbergservices.com, which included the following statement:

> ***Roth IRA calculators invariably assume someone has the cash and the intestinal fortitude to pay the additional tax due on conversion and they and their children will not be in lower tax brackets, which is often not the case. Conversions make less financial sense if a taxpayer must incur capital gains to raise the cash, or worse, use traditional IRA funds. Congress shut down the Roth segregation conversion strategy, which exploited the prior ability to cherry pick and "undo" (recharacterize) some Roth IRA conversions but not others. Taxpayers are not idiots to ask the question: "if Congress can suddenly pull the rug out from under "stretch IRAs" that we've relied on in planning for decades, what's to stop them from doing the same to Roth accounts?" The simple answer to this is "nothing." There is no Constitutional prohibition to changing the tax law. The SECURE Act was an astonishingly bipartisan bill. Unlike insurance companies, drug companies, real estate developers etc., there is no strong lobbying constituency to protect such broad tax breaks.***
>
> ***If a Roth conversion did not make sense when the beneficiaries could get 50-80 years of tax-free growth, it won't make much more sense when it's only ten years. Despite the above concerns, partial or even full Roth conversions can still make sense, but the variables to consider are often much more complicated than financial writers make them out to be. We are stuck with planning for traditional accounts for the foreseeable future.***

Eligible Rollovers

Most pre-retirement payments received from an IRA/Plan can be "rolled over" by depositing the payment into another IRA/Plan within sixty days; however, Internal Revenue Code Section 408(d)(3)(B) provides that there can be only one tax-free rollover by an individual within a twelve month period.[16]

Such transfers can also be completed by a financial institution or the retirement plan administrator directly to the new IRA/Plan custodian as a "trustee to trustee" rollover, without regard to the limitation of one tax-free rollover per twelve month period, because a "trustee to trustee" transfer does not constitute a rollover.

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[15] See The Ultimate Roth IRA Conversion Guide – Everything You Need to Know by Jeff Rose, CFP dated March 10, 2020, goodfinancialcents.com\roth-ira-conversion-tax-rules\ and Should I Do a Roth Conversion? By Roger A. Young, CFP, Kiplinger.com.

[16] *Bobrow v. Commissioner* confirmed this in 2014 when it severely penalized a taxpayer that attempted to roll over multiple IRAs in one calendar year.

The benefit of a rollover IRA/Plan is that a Plan Participant generally will not have to pay taxes on the IRA/Plan until he or she withdraws from the new IRA/Plan. In other words, by rolling over, the Plan Participant can save for his or her future and the contributed money will continue to grow tax deferred.

An eligible rollover distribution does not include:

1. Any distribution that is one of a series of substantially equal periodic payments made (at least annually) for:

    a. The life (or life expectancy) of the employee, or the joint lives (or joint life expectancies) of the employee and the Designated Beneficiary, or

    b. A specified period of ten years or more;[17]

2. Any distribution to the extent it is a Required Minimum Distribution; or

3. Any hardship distribution.

An eligible rollover distribution from a qualified plan is subject to 20% withholding, unless there is a direct trustee-to-trustee transfer. Plan administrators must inform recipients of potential rollovers of the applicable rollover rules in writing, known as a "Section 402(f) notice," no less than thirty days and no more than ninety days before making an eligible rollover distribution.

As discussed in Chapter 9, the CARES Act eliminates the requirement that a Required Minimum Distribution be made for 2020. Thus, a Plan Participant or IRA/Plan beneficiary who has not yet taken his or her 2020 Required Minimum Distribution is relieved of the obligation to do so. A Plan Participant, a Surviving Spouse who has rolled over the Plan Participant's IRA/Plan into his or her own IRA, or any beneficiary of an IRA/Plan who has already taken all or a portion of his or her 2020 Required Minimum Distribution may be eligible to rescind such Distribution, as described above.

Specifically, if an eligible rollover distribution is recontributed to the IRA/Plan before August 31, 2020, then such recontribution is treated as a rollover to effectively rescind the 2020 Required Minimum Distribution that was previously received. While any distribution that is a Required Minimum Distribution ordinarily cannot be recontributed to an IRA/Plan, because Required Minimum Distributions have been eliminated for 2020, any such prior distributions are not characterized by the IRS as Required Minimum Distributions.

Neither a "trustee-to-trustee" transfer described above nor a recontribution of a previously taken 2020 Required Minimum Distribution by a Plan Participant or a beneficiary thereof (regardless of whether the beneficiary is the Surviving Spouse of the Plan Participant) counts for the purposes of determining whether a tax-free rollover has been completed within the 12-month period.

[17] I.R.C. §402(c)(A)(4).

Do Not Forget Creditor Protection

Many states have laws which provide for the protection of IRA accounts from most categories of creditors, and some states have laws which protect inherited IRAs.

The U.S. Supreme Court decision of *Clark v. Rameker*[18] determined that federal bankruptcy law will not protect inherited IRAs for those residing in states that do not have exemption statutes for them.[19]

IRAs payable to Accumulation Trusts normally will be protected from creditors of the beneficiaries of the trusts, depending upon design, the category of creditor, and applicable law.

This, and further creditor protection planning for IRA and other Qualified Retirement Plans, is discussed in detail in Chapter 6.

Qualified Domestic Relations Orders (QDROs) In Divorce

IRA/Plans will normally not be transferrable between spouses, except upon death or divorce. To transfer an account to a spouse, child, or other person tax-free as the result of a divorce, it is necessary for the divorce court to issue a QDRO. These can be very complicated instruments.

Essentially, a QDRO is a domestic relations order that is a court decree, judgment, or order (including an approval of any property settlement) which creates an alternate payee who has a "right to receive, or assign to an alternate payee the right to receive, all or a portion of the benefits payable with respect to a Plan Participant under a retirement plan."[20] In a QDRO, the alternate payee may only be a spouse, former spouse, child, or other dependent of the individual recognized by the order.[21]

A QDRO must contain the following information:

- The name and last known mailing address of the Plan Participant and each alternate payee;
- The name of each Plan to which the order applies;
- The dollar amount or percentage (or the method of determining the amount or percentage) of the benefit to be paid to the alternate payee; and
- The number of payments or time period to which the order applies.

A QDRO may not impose any of the following requirements:

[18] *Clark v. Rameker*, 573 U.S. 122 (2014).
[19] See LISI Asset Protection Planning Newsletter #250 (June 26, 2014) at http://www.leimbergservices.com written by Christopher J. Denicolo, Alan S. Gassman and Brandon L. Ketron entitled *Clark v. Rameker*, 573 U.S. 122 (2014).
[20] I.R.C. § 414 (p)(1)(A).
[21] I.R.C. § 414 (p)(1)(B).

- That the Plan provide the alternate payee or other Plan Participant with any benefit or option that is not provided under the Plan;
- That the Plan provide for increased benefits based on actuarial value;
- That the Plan pay benefits to an alternate payee that is different than an alternate payee previously determined by a different QDRO order; or
- That a Plan provide benefits to the alternate payee in a form of "a qualified joint and survivor annuity for the lives of the alternate payee and/or his or her subsequent spouse."[22]

2019 Pronouncement on Canadian Registered Retirement Savings Plans (RRSPs) and Registered Retirement Income Funds (RRIFs)[23]

Plan Participants who hold RRSPs and/or RRIFs will now automatically qualify for tax deferral similar to U.S. IRA and 401(k) funds. Previously, Canadian Plan Participants were required to file a Form 8891 in order to qualify for tax deferral. The IRS has now eliminated Form 8891, and Plan Participants are no longer required to file this form for any year, past or present.[24]

Grandfather Rules for Pre-1984 IRAs and Pre-1987 403(b) Plans

The 1982 changes to the Tax Equity and Fiscal Responsibility Acts ("TEFRA") significantly affected the Required Minimum Distribution ("RMD") rules. For example, if an individual established an IRA prior to January 1, 1984, then Section 242(b) of TEFRA would allow that individual's Plan Participants to use the more liberal rules that applied before 1984. These rules include the option to postpone Required Minimum Distributions past the Required Beginning Date until retirement, regardless of whether the Plan Participant owns more than 5% of the company. The pre-1984 rules also exempt death benefits from the 5-year rule.

Also note that if separately identified, pre-1987 403(b) Plan balances are not subject to the Tax Reform Act of 1986, which applied the Required Minimum Distribution Rules to 403(b) Plans for the first time. If Plan Participants are lucky enough to benefit from the prior rules, here are some advantages to be aware of:

- The Required Beginning Date is the later of retirement or age 75.
- The required distributions are computed using the incidental death benefits rule.[25]
- If the Plan Participant dies on or before his or her Required Beginning Date, there are no requirements for how rapidly the death benefits must be distributed.[26]

[22] I.R.C. § 414 (p)(4)(A)(iii).
[23] Article 18 of the U.S.-Canada Income Tax Treaty.
[24] Rev. Proc. 2014-55, 2014-2 C.B. 753.
[25] See Treas. Reg. § 1.403(b)-6(e)(6).
[26] Choate – Life and Death Planning for Retirement Benefits 1.4.05.

Prohibited Transactions and LLCs Owned Under IRA

Generally, an IRA must be invested in traditional categories of assets. For example, investments in life insurance, certain types of derivative positions, antiques, collectibles, and most coins[27] are prohibited.

However, IRA trustees are permitted to impose additional restrictions on investments. For example, while the IRS does not prohibit an IRA from investing in real estate, most IRA custodians do not permit individualized real estate investments. Many taxpayers will find a flexible custodian that will allow the taxpayer to establish an LLC held by the custodian and managed by the taxpayer to invest in real estate and certain other vehicles. This can be very dangerous, and the penalties are severe. Another variety of individualized invested IRA is the ROBS, which stands for Rollovers as Business Startups. The authors' article entitled "*Can I Use My IRA to Start a Business? Maybe, But With Great Power, Comes Great Responsibility*"[28] was published on February 7, 2017, and can be found at Appendix F. Please do not "try this at home!"

The IRA custodian can allow the IRA owners to invest in alternative arrangements, if properly structured. Strict rules still apply, and the owner risks having the IRA lose its tax-deferred status if these rules are violated.

A prohibited transaction occurs when the IRA directly or indirectly engages in a transaction with a disqualified person, which is defined to include the following:

1. The IRA owner;
2. The IRA owner's spouse;
3. Any of the IRA owner's ancestors;
4. Any of the IRA owner's lineal descendants;
5. Any spouse of the IRA owner's lineal descendants;
6. Investment advisors;
7. The IRA custodian or trustee; or
8. Certain entities in which the IRA owner owns at least a 50% interest, such as a corporation, partnership or trust.

[27] Certain exceptions apply to coin collections: One, one-half, one-quarter or one-tenth ounce U.S. gold coins (American Gold Eagle coins) are the only gold coins specifically approved for IRAs. Other gold coins, to be eligible as IRA investments, must be at least .995 fine (99.5% pure); one ounce silver coins minted by the Treasury Department; any coin issued under the laws of any state; a platinum coin described in 31 U.S.C. § 5112(k) ; and gold, silver, platinum or palladium bullion (other than bullion that is made into a coin) of a certain fineness that is in the physical possession of a trustee that meets the requirements for IRA trustees under I.R.C.§ 408(a).

[28] LISI Employee Benefits & Retirement Planning Newsletter #668 (February 7, 2017) at http://www.leimbergservices.com.

A prohibited transaction also occurs when one of the following events has transpired:

- Sale, exchange, or leasing of any property occurs between the IRA and a disqualified person;
- There is lending of money or other extension of credit between the IRA and a disqualified person;
- There is a furnishing of goods, services or facilities between the IRA and a disqualified person;
- The assets are transferred to, or used by or for the benefit of, a disqualified person;
- Any action by a disqualified person who is a fiduciary whereby the fiduciary deals with the income or assets of the IRA in his or her own interests or for his or her own account; or
- Receipt of any consideration by Plan Participant from any disqualified person who is a fiduciary dealing with the plan in connection with a transaction involving the income or assets of the plan.[29]

The penalty for engaging in a Prohibited Transaction under an IRA is that the IRA ceases to be considered a retirement account and is treated as having been distributed on the first day of the taxable year in which the Prohibited Transaction occurred. It is important to note that the entire account is treated as distributed and not just the portion of the account that involves the Prohibited Transaction. If the Prohibited Transaction is not corrected prior to the end of the taxable period, then an additional 100% tax on the amount involved is imposed! It is therefore vitality important to avoid Prohibited Transactions and to have them corrected as soon as possible in order to avoid the harsh penalties associated therewith. For non-IRA retirement plans, the penalty for engaging in a Prohibited Transaction is not as harsh and there is only a 15% excise tax on the amount involved in a Prohibited Transaction.

It is therefore advisable to have any aggressive or client-controlled IRA custodian arrangement separated from other IRAs, so that only the assets involved with the client managed arrangement would become disqualified.

Access Before Age 59½

Individuals may withdraw monies from an IRA or SEP-IRA at any time, but amounts distributed other than from a Roth IRA generally will be includible in taxable income and subject to a 10% additional excise tax if the withdrawing Plan Participant is under age 59½, unless the distribution qualifies to avoid this excise tax for distributions not exceeding $100,000 in 2020 for certain qualified individuals under the CARES Act (a "Coronavirus-Related Distribution," as defined in Chapter 2),[30] or one of the exceptions below applies. Additionally, if the Plan Participant

[29] For potential sample Operating Agreement language see Appendix B.

[30] An individual under age 59½ is eligible for such an excise tax-free distribution if he or she: (a) is diagnosed with the virus SARS-CoV-2 or the disease COVID-19 by a test approved by the Centers for Disease Control and Prevention

withdraws money from a SIMPLE IRA within two years of creating it, there is an additional 25% tax.

There are a number of exceptions from the 10% excise tax. The most noteworthy are as follows:[31]

1. Automatic Enrollment – certain plans (Qualified Plans, SIMPLE IRAs, and SARSEPs) allow for permissible withdrawals.

2. Death – after death of the Plan Participant or IRA owner.

3. Disability – Plan Participant has a total and permanent disability.

4. Education – qualified higher education expenses are exempt from the tax (only applicable to IRAs, SEP IRAS, SIMPLE IRAs, and SARSEPs, and not Qualified Plans).[32]

5. Equal Payments – series of substantially equal payments.

6. Birth or Adoption – a Plan Participant can withdraw up to $5,000 within one year of the birth or adoption of a child. This exception was recently enacted under the SECURE Act.

7. First Time Homebuyers – qualified first-time homebuyers may receive an exemption up to $10,000 (only applicable to IRAs, SEP IRAS, SIMPLE IRAs, and SARSEPs, and not Qualified Plans).

8. Levy – because of an IRS levy of the plan.

9. 60 Day Rule - any money can be withdrawn temporarily, as long as the money is placed back into the account within sixty days of the withdrawal.

10. Medical Expenses - the Plan Participant has unreimbursed medical expenses that are more than 10% (or 7.5% if the Plan Participant or his or her spouse was born before January 2, 1949) of his or her adjusted gross income.

11. Medical Insurance - the distributions are not more than the cost of Plan Participant's medical insurance during a period of unemployment.

(CDC); (b) has a spouse or dependent who is diagnosed with the virus or disease by such a test; or (c) experiences adverse financial consequences as a result of being quarantined, being furloughed or laid off or having work hours reduced due to such virus or disease, being unable to work due to lake of childcare due to such virus or disease, closing or reducing hours of a business owned or operated by the individual due to such virus or disease, or other factors as determined by the Secretary of the Treasury (or the Secretary's delegate).

[31] https://www.irs.gov/retirement-plans/plan-participant-employee/retirement-topics-tax-on-early-distributions (last visited on June 21, 2020).

[32] Qualified Education Expenses include tuition, fees, books, supplies, and equipment required for enrollment or attendance at an eligible educational institution. In addition, if the student is at least a half-time student, room and board are qualified education expenses.

12. Military – certain distributions to qualified military reservists called to active duty.

13. Returned IRA Contributions – if withdrawn by the extended due date of the applicable tax return (only applicable to IRAs, SEP IRAS, SIMPLE IRAs, and SARSEPs, and not Qualified Plans).

14. Rollovers – in-plan Roth rollovers or eligible distributions contributed to another retirement plan or IRA within sixty days.

Inherited IRAs (whether held in trust or outright) are subject to different rules. Minimum Distribution Rules will apply as discussed in more detail in the chapters that follow.

Access Between Age 59½ and the Required Beginning Date

Once the Plan Participant reaches the age of 59½, withdrawals can be made from the IRA but are not required.

Each withdrawal from a traditional IRA is taxable as ordinary income unless: (1) the withdrawal is rolled over within sixty days (only one rollover is permitted per year per Plan Participant under the *Bobrow v. Commissioner* case, discussed in Appendix C); or (2) to the extent considered to be a return of a nondeductible contribution.

The Cream in the Coffee Situation (Partly Taxable Distributions)

Basis (investment in the contract) is received for any non-deductible contributions or rolled-over after-tax amounts made into an IRA/Plan. Until the Plan Participant's entire basis has been distributed, each distribution is partly non-taxable and partly taxable.

The taxable and non-taxable portions are determined by the following formula:

Total Basis in the Contract ***x Distribution Amount – Total Value of the Contract***

After the Required Beginning Date

A Plan Participant who has reached the Required Beginning Date must withdraw the Required Minimum Distribution amount by December 31st of each year, other than for 2020, to avoid paying penalties that can be at least 50% of the amount that should have been withdrawn. A Plan Participant who has reached the Required Beginning Date can withdraw more than the minimum without penalty, and all withdrawals will be included in taxable income, unless the Plan Participant has made non-deductible contributions to the IRA and a portion is considered tax-free. The Required Minimum Distribution rules apply during the lifetime of the Plan Participant, and/or to a Surviving Spouse who has rolled over an inherited IRA as a direct beneficiary thereof, based upon such Surviving Spouse's Required Beginning Date.

To calculate a Plan Participant's minimum distribution, there are two potential formulas:

1. The first applies only if the Plan Participant has designated his or her spouse as the sole beneficiary and such spouse is more than ten years younger than the Plan Participant; and

2. The second applies for everyone else.

If the Plan Participant's spouse is ten years younger than the Plan Participant and is designated as the sole beneficiary of the IRA/Plan, then the Required Minimum Distribution calculation is based upon the combined life expectancy of both the Plan Participant and his or her spouse. To calculate the distribution, the Plan Participant would take his or her IRA account balance as of December 31st of the previous year and divide it by the life expectancy indicated at the intersection of the Plan Participant's age and his or her spouse's age on the Joint Life and Last Survivor Expectancy Table. This is discussed in more detail in Chapter 4.

If a Plan Participant's spouse is not ten or more years younger than the Plan Participant, or is not designated as the sole beneficiary of the IRA/Plan (or as a beneficiary of the IRA/Plan to any extent), then the Required Minimum Distribution is based solely on the Plan Participant's life expectancy. To calculate the Required Minimum Distribution, he or she will take the IRA balance on December 31st of the previous year and divide it by the life expectancy indicated on the Uniform Life Table. This is discussed in more detail in Chapter 4.

If no distributions are taken, or if the distributions are too small, then the Plan Participant may have to pay at least a 50% excise tax on the amount not distributed.

Generally, once a Plan Participant reaches the Required Beginning Date, the Plan Participant is required to withdraw the Required Minimum Distribution from the account each year, other than in 2020, but there are exceptions to the general rule.

First, no withdrawal is required from a Roth IRA until after the death of the owner. The second exception is for a Plan Participant in a Qualified Pension Plan, or if the Plan Participant's IRA allows such Plan Participant to wait until the year he or she actually retires to take the first Required Minimum Distribution (often referred to as "RMDs"). In these cases, the Required Minimum Distribution can be delayed for a period of time, typically being one year following his or her retirement. Additionally, if a Plan Participant owns 5% or more of the business sponsoring the Qualified Retirement Plan, he or she must begin receiving distributions by April 1st of the year after he or she reaches the Required Beginning Date, even if the Plan Participant has not retired.

Furthermore, the 2015 Protecting Americans from Tax Hikes (PATH) Act made the IRA Qualified Charitable Distribution permanent. The IRA Qualified Charitable Distribution (often referred to as the "QCD") allows an individual who has reached the age of 70½ to have up to $100,000 pass directly from his or her IRA to a qualified charity, without having to treat the distribution as having been taxable income or satisfying the percentage of adjusted gross income deductibility rule, which normally apply to individuals who contribute to charity. The SECURE Act did not increase the age requirement for this to 72 despite increasing the Required Beginning Date to age 72, so individuals who have reached the age of 70½ can take advantage of a Qualified Charitable Distribution.

It is noteworthy that the SECURE Act eliminated the prior law that prevented an individual who had reached age 70½ from making further IRA contributions, and that the $100,000 allowance for the Qualified Charitable Distribution will be reduced to the extent that the individual made IRA contributions after reaching age 70½, even if the IRA contributions are made in a tax year before the year that the Qualified Charitable Distribution is made. The reduction applies until the Qualified Charitable Distributions equal or exceed the preceding IRA contributions. All contributions and Qualified Charitable Distributions made in a calendar year are considered to have occurred simultaneously.

For example, a taxpayer could contribute $7,000 to his or her IRA after reaching the age of 70½ and provide for a $93,000 Qualified Charitable Distribution. As another example, if a taxpayer who turned 70½ in 2020 made a qualified contribution of $6,500 to her traditional IRA in 2021, and then donated $80,000 to charity using a Qualified Charitable Distribution in 2022, only $73,500 of such donation would qualify as a Qualified Charitable Distribution. Assuming that no further qualified contributions are made to the IRA in either example, future charitable donations of Required Minimum Distribution amounts up to $100,000 per year will qualify as Qualified Charitable Distributions.

The Qualified Charitable Distribution is an excellent tool for taxpayers to essentially obtain an income tax charitable deduction where he or she otherwise might not be entitled to do so if he or she is not itemizing deductions of his or her personal income tax return. This is because a taxpayer can take advantage of a Qualified Charitable Distribution to reduce his or her taxable income applicable to the Required Minimum Distribution, regardless of whether he or she is itemizing deductions. Nevertheless, taxpayers who are itemizing deductions might be better served by donating appreciated assets to charity rather than taking a Qualified Charitable Distribution if the Qualified Charitable Distribution does not have the effect of reducing or eliminating income tax on Required Minimum Distributions (i.e., the taxpayer's Required Minimum Distributions are less than the desired amount that the taxpayer wishes to give to charity, or in 2020, where generally Required Minimum Distributions are waived).

After Death of Plan Participant

A Surviving Spouse who is the sole Designated Beneficiary has a number of options on how to proceed and may use part of the inherited IRA/Plan for one or more of the below purposes if the applicable requirements are satisfied:

- Treat an IRA as his or her own by making a spousal rollover;
- Base Required Minimum Distributions on his or her own current age;
- Base Required Minimum Distributions on the decedent's age at death, reducing the distribution period by one each year, if the account owner died after his or her Required Beginning Date;
- Take Required Minimum Distributions based upon the mortality table life expectancy of the Designated Beneficiary, reducing the distribution period by one each year, with the entire account being withdrawn by the end of the 10th calendar year following the calendar year of the deceased Plan Participant's death.

Alternatively, if the Plan Participant died before his or her Required Beginning Date, withdraw the entire account balance by the end of the 10th calendar year following his or her death; or [33]

- Withdraw the entire account balance by the end of the 5th calendar year following the account owner's death, if the account owner died before his or her Required Beginning Date.

If the Plan Participant has died after 2019 but before his or her Required Beginning Date, then the Surviving Spouse can wait until the calendar year after the Plan Participant would have turned age 72 to begin receiving Required Minimum Distributions. If the Plan Participant died before 2020 and also before his or her Required Beginning Date, then the Surviving Spouse can wait until the calendar year after the Plan Participant would have turned age 70½ to begin receiving Required Minimum Distributions. In either case, no Required Minimum Distributions need to be made in 2020 as a result of the CARES Act. Therefore, if a Surviving Spouse (or any other beneficiary) otherwise would have had to begin receiving Required Minimum Distributions in 2020, then Required Minimum Distributions will not begin until 2021. Further, any Required Minimum Distributions which the Surviving Spouse (or any other beneficiary) would have had to receive in 2020 are eliminated under the CARES Act. Nevertheless, as confirmed by IRS Notice 2020-51, a Plan Participant whose Required Beginning Date is April 1, 2020 is still considered to have reached his or her Required Beginning Date on April 1, 2020, notwithstanding that no Required Minimum Distribution must be paid in 2020.

Surviving Spouse Exception

A Surviving Spouse named as beneficiary of a deceased Plan Participant's IRA/Plan who has not yet reached age 59½ may withdraw funds from the plan without being subject to the 10% excise tax, unless or until the IRA/Plan has been rolled over to the Surviving Spouse's own IRA. As to any portion of the IRA/Plan that the Surviving Spouse has rolled over into his or her own IRA, once a rollover IRA has been established and funded, the 10% excise tax will apply to any distributions from such rollover IRA that are made before the Surviving Spouse reaches the age of 59½ unless an exception applies.

This may be a good reason to delay making a complete rollover, or for the Surviving Spouse to only roll over a portion of the inherited IRA/Plan into his or her own IRA; however, the Surviving Spouse will not be able to change the beneficiary designation of the deceased Plan Participant's IRA/Plan if it is not rolled over. It is noteworthy that the Proposed Regulations issued on February 24, 2022 do not change the IRA rollover rules at all. Surviving Spouse may choose to roll over all or part of an inherited IRA of which he or she is the sole Designated Beneficiary at any time. Therefore, a Surviving Spouse who has not reached age 59½ may elect to take only what will be needed to provide for support and expected expenses up through age 59½ as an inherited IRA, and may roll the remaining amount over into his or her own rollover IRA.

[33] The Proposed Regulations discussed in detail in Chapter 8 surprised many practitioners by requiring that Required Minimum Distributions be made in each of the first nine years following the Plan Participant's death if he or she died after his or her Required Beginning Date, rather than simply being deferred for the entire 10-year period. It remains to be seen whether this will be revised in the Final Regulation.

Beneficiaries Other Than The Spouse

Individual beneficiaries other than a spouse and an Eligible Designated Beneficiary (as defined in Chapter 7) can:

- Withdraw the entire account balance by the end of the 10th calendar year following the account owner's death, if the account owner died before his or her Required Beginning Date, or

- If the Plan Participant died on or after his or her Required Beginning Date, the beneficiary may use the Plan Participant's life expectancy at death (if the Plan Participant had a longer life expectancy than 10 years), with the Applicable Divisor being reduced by one for each subsequent year.

Generally, Congress and the IRS have put a number of limitations on IRAs to ensure that they do not last indefinitely, including the recent passage of the SECURE Act. However, under Internal Revenue Code Section 401(a)(9), and the now inconsistent Treasury Regulations, certain trusts can be treated as having Designated Beneficiaries, and will thus be eligible for the 10-Year Rule, or to stretch post-death Required Minimum Distributions over the life expectancy of an Eligible Designated Beneficiary of the trust. This can be accomplished by creating a Conduit Trust or an Accumulation Trust, but in order to receive this protection the trust must be properly drafted and managed.

Prior to the enactment of the SECURE Act (which became effective January 1, 2020), the law provided that all assets held under a Retirement Plan must be distributed out of the plan under the 5-Year Rule, which is by December 31st of the 5th calendar year following the year of the Plan Participant's death, unless one of the of the following applied:

(a) The Plan Participant died after his or her Required Beginning Date, in which event the post-death required minimum distribution payments could be made over the life expectancy of the deceased Plan Participant as if he or she were still living; or

(b) The assets in the IRA/Plan will be distributed annually over the life expectancy of a Designated Beneficiary named by the deceased Plan Participant.

An adjustment to the 5-Year Rule was added by the 2020 CARES Act so that 2020 is not counted as having occurred for Required Minimum Distribution purposes, and thus converting the 5-Year Rule into a "6-Year Rule" for decedents who have died in the calendar years 2015 through 2019.

The ability to "stretch" Required Minimum Distributions from an IRA/Plan over a beneficiary's or the Plan Participant's life expectancy is known as the "Life Expectancy Rule." This Rule was the foundation for the pre-2020 "Stretch IRA" planning techniques which allowed for the deferral of distributions from an inherited IRA/Plan (and corresponding income tax burden associated with such distributions) over many years.

The major change to the above brought about by the SECURE Act, which is discussed in detail in Chapter 7, is that the Life Expectancy Rule has been replaced by a 10-Year Payout Rule, except in the case of IRA/Plans being left directly to an Eligible Designated Beneficiary or to a Conduit

Trust for an Eligible Designated Beneficiary or to an Accumulation Trust for a disabled or chronically ill Designated Beneficiary, or an Accumulation Trust benefitting certain beneficiaries (such as minor children). Therefore, the lifetime Stretch IRA for most non-spousal situations is no longer available, and instead all assets must be paid out from the IRA/Plan on or before the 10th anniversary of December 31st of the calendar year in which the Plan Participant dies. Interestingly, many practitioners believe that the 10-Year Rule would allow for properly situated IRA plan distributions to be deferred until the 10th year, which would have allowed for significant accumulations of assets and potentially caused many taxpayers to come out ahead based upon 10 years of tax deferral and the time value of money. Many practitioners were shocked when the Proposed Regulations were released interpreting the SECURE Act to require that distributions be made based upon the Designated Beneficiary's life expectancy and years one through nine with the entire account balance being liquidated in the 10th year following the death of the Plan Participant rather than 10 years of deferral. It remains to be seen if this will be modified when the Proposed Regulations become Final Regulations in late 2022 or early 2023.

Planning Pointer

It almost always makes sense to always withdraw remaining IRA/Plan assets on the first possible date in January of the calendar year in which all remaining distributions must occur; e.g., where the 5-Year Rule or 10-Year Rule applies to require all assets to be distributed from the IRA/Plan by the end of the 5th or 10th year, as applicable), so that post-distribution growth during the year will not be subject to income tax at ordinary rates with respect to growth in value and qualified dividends received during that last calendar year.

A chart comparing the primary payout methods Pre-SECURE Act and Post-SECURE Act is below:

PRIMARY PAYOUT METHODS PRE-SECURE ACT AND POST-SECURE ACT

Category of Beneficiary	Pre-2020 Law	Post-2019-SECURE Act
Surviving Spouse		
(a) Rollover IRA	Life Expectancy of Surviving Spouse recalculated annually, using the Uniform Life Table	May use deceased spouse's life expectancy if the Plan Participant was younger than the Surviving Spouse
(b) Inherited IRA	Life Expectancy of Surviving Spouse recalculated annually, using the Single Life Table	Same
(c) Conduit Trust – must pay all contributions to spouse	Life Expectancy of Surviving Spouse recalculated annually, using the Single Life Table	Same
(d) Accumulation Trust	Life Expectancy of Surviving Spouse not recalculated annually using the Single Life Table	Now, the 10-Year Rule will apply, unless Accumulation Trust meets an exception under the Proposed Regulations (so that the Life Expectancy payout rules of Pre-2020 law apply).

Category of Beneficiary	Pre-2020 Law	Post-2019-SECURE Act
Non-Spouse Beneficiary More Than 10 Years Younger Than Deceased Plan Participant – Not Disabled, Chronically Ill or a Minor Child of the Plan Participant		
(a) Payable directly to individual beneficiary	Life Expectancy of beneficiary – not recalculated annually using the Single Life Table	10-Year Rule applies
(b) Conduit Trust	Life Expectancy of conduit beneficiary – not recalculated annually using the Single Life Table	10-Year Rule applies, if trust qualifies as a See-Through Trust
(c) Accumulation Trust	Life Expectancy of oldest trust beneficiary – not recalculated annually using the Single Life Table	10-Year Rule applies, if trust qualifies as a See-Through Trust, unless Accumulation Trust meets an exceptions espoused by the Proposed Regulations (in which case the Life Expectancy payout rules of Pre-2020 law apply).
Child of the Plan Participant who is Under Age of Majority		
(a) Outright payment to child or custodian under Gift to Minors Act Account	Life Expectancy of beneficiary - not recalculated annually using the Single Life Table	Life Expectancy payout rules of Pre-2020 Law apply until reaching age of majority – 10-Year Rule applies beginning when child reaches age 21.
(b) Conduit Trust for Minor Child	Life Expectancy of conduit beneficiary – not recalculated annually using the Single Life Table	Same as above if trust qualifies as See-Through Trust
(c) Accumulation Trust for Minor Child	Life Expectancy of oldest trust beneficiary – not recalculated annually using the Single Life Table	Same as above, if trust qualifies as See-Through Trust
Non-Spouse Beneficiary Not More Than 10 Years Younger Than Deceased Plan Participant – Not Disabled, Chronically Ill or a Minor Child of the Plan Participant		
(a) Payable directly to individual beneficiary	Life Expectancy of beneficiary – not recalculated annually, using the Single Life Table	Same
(b) Conduit Trust	Life Expectancy of conduit beneficiary – not recalculated annually, using the Single Life Table	Same

Category of Beneficiary	Pre-2020 Law	Post-2019-SECURE Act
(c) Accumulation Trust	Life Expectancy of oldest trust beneficiary – not recalculated annually, using the Single Life Table	10-Year Rule applies, if trust qualifies as See-Through Trust, unless Accumulation Trust meets an exception espoused under the Proposed Regulations (so that the Life Expectancy payout rules of Pre-2020 law apply).
Individual Who is Disabled or Chronically Ill on Plan Participant's Date of Death		
(a) Payable directly to individual beneficiary	Life Expectancy of beneficiary – not recalculated annually, using the Single Life Table	Life Expectancy payout rules of Pre-2020 Law
(b) Conduit Trust	Same as above	Same as above, if qualifies as See-Through Trust
(c) Accumulation Trust	Same as above	Same as above, if qualifies as See-Through Trust

While the Stretch IRA has been significantly curtailed by the SECURE Act for most non-spousal situations and for spousal Accumulation Trusts, the concept of a "Designated Beneficiary" is alive and well, although not always as important. A "Designated Beneficiary" is an individual named as beneficiary of the IRA/Plan. Where a certain type of trust qualifies as a "See-Through Trust," the oldest trust beneficiary generally is considered to be the Designated Beneficiary. However, the 2022 Proposed Regulations introduced the concepts of "Tier I Beneficiaries," "Tier II Beneficiaries," and "Tier III Beneficiaries," which have greatly simplified the determination of Designated Beneficiaries under the Required Minimum Distribution rules.

A Tier I Beneficiary is any beneficiary who could receive a distribution from the trust that can be paid from a portion of the IRA/Plan, and whose interest is neither contingent upon, nor delayed until, the death of another trust beneficiary who survived the Plan Participant. In other words, a Tier I Beneficiary can receive a distribution of IRA/Plan assets that are held under a See-Through Trust. Tier I Beneficiaries who have such status on or after September 30 of the year following the calendar year of the deceased Plan Participant's death always count for Designated Beneficiary determination purposes, regardless of whether the trust is a Conduit Trust or an Accumulation Trust.

A Tier II Beneficiary is a beneficiary of a See-Through Trust who could receive a distribution from the trust from a portion of the IRA/Plan, but only after the death of a Tier I Beneficiary. Tier II Beneficiaries who have such status on or after September 30 of the year following the calendar year of the deceased Plan Participant's death count only in an Accumulation Trust, but not in a Conduit Trust; however, Tier II Beneficiaries do not count in an Accumulation Trust if a minor child is the sole Tier I Beneficiary and the trust provides for all assets to be distributed outright to the minor upon reaching the age of 31 (the Minor Child Accumulation Trust Exception, which is described below).

A Tier III Beneficiary is any beneficiary who could receive a distribution from the trust from a portion of the IRA/Plan solely because of the deaths of all Tier I Beneficiaries and all Tier II Beneficiaries. In other words, a Tier III Beneficiary cannot benefit from the IRA/Plan assets under the trust unless and until after the death or other elimination of all Tier I Beneficiaries and all Tier II Beneficiaries. Tier III Beneficiaries never count for Designated Beneficiary determination purposes!!!

As a result of the above, trusts can now safely provide that creditors, charities and individuals older than the Primary Beneficiary can be "contingent remainder beneficiaries" (i.e., Tier III Beneficiaries) as long as there are at least two people who will first benefit while they are living, and the "contingent remainder beneficiaries" can only benefit after the death of the first two beneficiaries.

Further, the 2022 Proposed Regulations provide that when all Tier I Beneficiaries and Tier II Beneficiaries are Eligible Designated Beneficiaries, the minimum Accumulation Trust can qualify for the Life Expectancy Rule whereby the life expectancy of such Eligible Designated Beneficiary will apply for the purposes of determining the Required Minimum Distribution payout. It is important that any such Accumulation Trust is appropriately drafted so that only Eligible Designated Beneficiaries will be Tier I or Tier II Beneficiaries of the trust to help ensure that life expectancy distributions will apply in lieu of the 10-Year Rule.

Nevertheless, trusts which will receive IRA/Plan benefits will still need to qualify as "See-Through Trusts," although under the more flexible "Beneficiary Tiers" rules that have been espoused by the Proposed Regulations. Accordingly, a trust which is intended to receive IRA/Plan assets must have special provisions to allow the trust to qualify as a See-Through Trust in order to be able to take advantage of the 10-Year Rule, or in some circumstances, the Life Expectancy Rule. This includes the necessity of being able to identify who the oldest individual beneficiary of a trust is, even though the age of that beneficiary may no longer have any impact on distributions when the 10-Year Rule applies. If such a trust does not have the special provisions that are required for a See-Through Trust, then the default 5-Year Rule (or the At-Least-As-Rapidly Rule) will apply.

Pension Planning Considerations

The SECURE Act changed the playing field for many taxpayers who are able to continue to work past age 70½, and may wish to maximize income tax deferral, and in some situations for charitable planning.

For example, the SECURE Act changed the previous rule that required a pension or profit-sharing plan to be signed by December 31st of the calendar year for S corporation, partnership and other calendar year business entities. Such entities will now have until September 15th of the following year, provided that such entity files an extension for its 1120-S, 1065 or 1040 returns, to implement a pension or profit-sharing plan that can apply for the previous year, and be funded by the due date of the entity tax return, taking into account the advantage of any extensions.

The funding of a pension plan can facilitate avoidance or elimination of the Internal Revenue Code Section 1411 Medicare Tax, and unlike contributions to deductible IRAs after age 70½, contributions to pensions and profit-sharing plans will not reduce the $100,000 annual Qualified Charitable Distributions that will otherwise apply to IRAs, as further discussed in Chapter 5.

An individual who is past age 70½ can fund up to $62,000 per year under a 401(k) or profit-sharing plan, up to $254,000 per year to a defined benefit plan, or up to $261,000 per year to a cash balance plan, as shown in the chart below.[34]

COMPARISON OF MAXIMUM CONTRIBUTIONS			
	Defined Contribution	**Defined Benefit**	**Maximum Contribution for a Cash Balance Plan**
Employee age 60	$62,000	$254,000	$261,000
Employee age 55	$62,000	$194,000	$203,000
Employee age 50	$62,000	$148,000	$158,000
Employee age 45	$56,000	$113,000	$123,000
Employee age 40	$56,000	$ 87,000	$ 96,000

Permanency Requirement – A defined benefit or cash balance plan must be "permanent," which normally means that it will be in place at least five years, unless there are circumstances beyond the reasonable control of the Employer.

Anticipates 401(k) plan catch-up contributions.

Please note: The above numbers are approximations. Actual results will vary based on actual census data, plan assumptions, and plan experience.

The authors thank Stephen Evers at Ascensus TPA Solutions for providing us with this chart.

Planners can use the census form provided below to request that a qualified actuary run numbers on whether a taxpayer should continue, establish or terminate existing plans, and make changes or establish new ones.

[34] The numbers will be updated when the next edition of the book is released, which will be shortly after the Proposed Regulations are finalized.

EMPLOYEE CENSUS FORM

Name of Employer: ______________________________

Provide complete information for all employees employed during the year, even if they have terminated.

Employee Name	Date of Birth	Date of Hire	Date of Termination	Annualized W-2 Compensation	Hours Per Week	Ownership Percentage

The third chart below provides an example of the significant amounts that may be contributed for key highly compensated employees, and the relatively low amounts that may be contributed to non-highly compensated employees to satisfy the pension non-discrimination rules.

JOHN SMITH
A Combination 401(k) / Profit Sharing / Cash Balance Plan
For the Plan Year 01/01/2017 – 12/31/2017

CONTRIBUTION REPORT – DETAIL

							Cash Balance		Profit Sharing		Total Contribution				
POH	Class	Last Name	First Name	AA	RA	Considered Earnings	Amount	%	Amount	%	Amount	%	Employer Cost	%	Total
…	A	Smith	John	56	65	270,000	198,369	73.5	8,100	3.0	206,469	76.5	206,469	76.5	94.2
	B	Jones	Tom	27	65	22,724	909	4.0	1,932	8.5	2,840	12.5	2,840	12.5	1.3
	B	Doe	Jane	37	65	28,948	1,158	4.0	2,461	8.5	3,618	12.5	3,618	12.5	1.7
	B	White	Amy	47	65	24,394	976	4.0	2,073	8.5	3,049	12.5	3,049	12.5	1.4
	B	Adams	Martha	39	65	25,284	1,011	4.0	2,149	8.5	3,160	12.5	3,160	12.5	1.4

Legend: P-Principal, O-Owner, H-Highly Compensated Employees

CONTRIBUTION REPORT – SUMMARY

		Cash Balance		Profit Sharing		Total Contribution				
	Considered Earnings	Amount	%	Amount	%	Amount	%	Employer Cost	%	Total
Principals	270,000	198,369	73.5	8,100	3.0	206,469	76.5	206,469	76.5	94.2
Non-Principals	101,350	4,054	4.0	8,615	8.5	12,669	12.5	12,669	12.5	5.8
Grand Total	**371,360**	**202,423**	**54.5**	**16,715**	**4.5**	**219,138**	**59.0**	**219,138**	**59.0**	**100.0**

CHAPTER 2 –
PLAYERS AND DEFINITIONS

The most challenging yet easily overcome obstacle to understanding IRA/Plan rules and techniques is the terminology that needs to be understood to navigate in this area.

Below we have enumerated primary definitions, terms, and a number of the basic rules that apply thereto. This Chapter is intended to permit the user to first refresh his or her memory to assure that the user has an understanding of these basic concepts, and then also provide a place that the reader can come back to for reinforcement thereof. First, we discuss the "PLAYERS" and then we review "CRUCIAL RULES." Readers who are new to this area are encouraged to become acquainted with what we have provided here, and much of this will be reinforced and built upon in subsequent Chapters, which refer back to these definitions and primary rules to enable those who skip ahead or use this Book on a periodic basis, as and when needed.

The definitions, which arose or became formalized under the SECURE Act and the Proposed Regulations issued on February 24, 2022 are as follows:

1. Chronically Ill
2. Disabled
3. Eligible Designated Beneficiaries
4. 10-Year Rule
5. See-Through Trust
6. Conduit Trust
7. Accumulation Trust
8. Tier I Beneficiaries; Tier II Beneficiaries; and Tier III Beneficiaries

We have put all post- and presently applicable pre-SECURE Act definitions under this Chapter, as enumerated below.

Additionally, the CARES Act has introduced the new term "Coronavirus-Related Distribution" as part of the exception to the 10% excise tax that applies if a Plan Participant, or a Surviving Spouse named as beneficiary of a deceased Plan Participant's IRA/Plan who has not rolled over the Plan Participant's IRA/Plan into his or her own IRA, withdraws assets from the IRA/Plan before he or she reaches the age of 59½.

I. <u>Players</u>

1. IRA/Pension Plan/Retirement Plan accounts. For the purposes of this Book, we use these terms interchangeably, and will most commonly refer to them as an "IRA/Plan" or "IRA/Plans."

Many IRA/Plan custodians limit beneficiary designation rights, sometimes necessitating rollover to an IRA that will permit the desired planning configuration, whether before or after the death of the Plan Participant.

The actual technical names given to the various plans that come under these rules are as follows:

(a) Traditional IRA;

(b) SIMPLE IRAs;

(c) Simplified Employee Pension (SEP);

(d) Employer sponsored retirement plans, such as 401(k) plans, defined benefit plans, defined contribution plans, and profit-sharing plans;

(e) 403(b) plans;

(f) 457(b) plans;

(g) Roth 401(k) plans;

(h) Roth IRAs, however, Roth IRAs are not subject to the Required Minimum Distribution rules until the owner of the Roth IRA (or the spouse of the deceased owner who rolled over into his or her own Roth IRA) dies; and

Almost any of the above plans can be transferred to another of the above plans during the life of a Plan Participant. An IRS chart (Illustration 2.0) released on November 17, 2014 can be found on the following page, as featured in Leimberg Information Services Tax Tips, November 24, 2014.

The term "Qualified Retirement Plan" is used to denote IRA/Plans that are not IRAs, such as employer sponsored retirement plans [401(k)s], defined benefit plans, defined contributions plans, cash balance plans, simple plans, profit-sharing plans, 403(b) plans and 467 plans.

Also see Appendix C for an article by the authors entitled "*Bobrow Raises Brows*" discussing the limitations on rollovers after *Bobrow v. Commissioner*, which held that a Plan Participant is only allowed to roll over one IRA in a calendar year and that erroneous IRS instructions could not be relied upon.

ROLLOVER CHART

Roll From \ Roll To	Roth IRA	Traditional IRA	SIMPLE IRA	SEP-IRA	Governmental 457(b)	Qualified Plan[1] (pre-tax)	403(b) (pre-tax)	Designated Roth Account (401(k), 403(b) or 457(b))
Roth IRA	Yes[2]	No	No	No	No	No	No	No
Traditional IRA	Yes[3]	Yes[2]	Yes[2,7], after two years	Yes[2]	Yes[4]	Yes	Yes	No
SIMPLE IRA	Yes[3], after two years	Yes[2], after two years	Yes[2]	Yes[2], after two years	Yes[4], after two years	Yes, after two years	Yes, after two years	No
SEP-IRA	Yes[3]	Yes[2]	Yes[2,7], after two years	Yes[2]	Yes[4]	Yes	Yes	No
Governmental 457(b)	Yes[3]	Yes	Yes[7], after two years	Yes	Yes	Yes	Yes	Yes[3,5]
Qualified Plan[1] (pre-tax)	Yes[3]	Yes	Yes[7], after two years	Yes	Yes[4]	Yes	Yes	Yes[3,5]
403(b) (pre-tax)	Yes[3]	Yes	Yes[7], after two years	Yes	Yes[4]	Yes	Yes	Yes[3,5]
Designated Roth Account (401(k), 403(b) or 457(b))	Yes	No	No	No	No	No	No	Yes[6]

[1]Qualified plans include, for example, profit-sharing, 401(k), money purchase, and defined benefit plans.
[2] Only one rollover in any 12-month period.
[3]Must include in income.
[4]Must have separate accounts.
[5]Must be an in-plan rollover.
[6]Any nontaxable amounts distributed must be rolled over by direct trustee-to-trustee transfer.
[7]Applies to rollover contributions after December 18, 2015. For more information regarding retirement plans and rollovers, visit Tax Information for Retirement Plans.

2. Person. A living individual. The term "Person" does not include an entity (such as a corporation, partnership, or LLC), an estate, or a trust, regardless of whether the trust or entity is considered to be "disregarded" and treated as owned by an individual under the "Defective Grantor Trust" rules or otherwise under the tax law.

3. Non-Person Beneficiary. An estate, charity, company, corporation, partnership, LLC, trust or other "non-individual" named as the direct beneficiary of an IRA/Plan, or a non-individual that is the beneficiary of a trust to which an IRA/plan is made payable.

4. Plan Participant. The person who is the IRA owner or Qualified Retirement Plan participant, while alive, or after death.

5. Beneficiary. The Person, trust, or other entity named as the direct beneficiary of an IRA/Plan or the person who will inherit directly upon the death of the Plan Participant.

6. Non-Spouse Beneficiary. Any Beneficiary other than the Plan Participant's spouse.

7. Surviving Spouse. The person married to the Plan Participant is his or her Spouse. The person married to the Plan Participant on his or her death is the Surviving Spouse. We are using these terms interchangeably.

   Note - Federal law (ERISA) gives the Surviving Spouse an absolute right to be considered the sole beneficiary of certain Qualified Retirement Plans of his or her spouse, unless this right has been legally waived.[35]

8. *Bobrow* Problem. The January 28, 2014 Tax Court Decision of *Bobrow v. Commissioner* shocked a great many advisors by holding that a Plan Participant who followed an apparently inaccurate IRS Publication (Publication 590) who made two "tax-free rollovers" during a single year was penalized when the IRS guidance he followed was not permitted under Internal Revenue Code Section 408(d)(3)(B), which only permits one rollover per calendar year.

   This case is discussed in Appendix C and casts at least a light gray cloud on much of the conventional wisdom in this area.

[35] This spousal waiver requirement can be satisfied by an appropriate document signed by the Plan Participant's spouse before or after the Plan Participant's death and will apply to plans covered by ERISA. The waiver requirement will probably not be satisfied by the execution of a prenuptial agreement or an agreement to execute a waiver, because these types of agreements will not satisfy the applicable consent requirements. Nuptial agreements may provide that to the extent the nonparticipating spouse fails to release his or her claims to retirement plan benefits, the heirs of the participant spouse may have a cause of action.

The Bobrow Problem was fixed, but only as to incorrect FAQs and certain other IRS guidelines by an October 15, 2021 news release[36] issued by the IRS in an attempt to address concerns regarding the application of penalties to taxpayers who rely on FAQs. This update provides that FAQs can be relied upon for reasonable cause defenses against negligence or other accuracy-related penalties to the extent that the reliance results in an underpayment of tax, and that any guidance published on the Internal Revenue Bulletin may also be used as precedent:

> [I]f a taxpayer relies on any FAQ (including FAQs released before today) in good faith and that reliance is reasonable, the taxpayer will have a "reasonable cause" defense against any negligence penalty or other accuracy-related penalty if it turns out the FAQ is not a correct statement of the law as applied to the taxpayer's particular facts.

It is important to note that the IRS was careful to add that “if an FAQ turns out to be an inaccurate statement of the law as applied to a particular taxpayer's case, the law will control the taxpayer's tax liability,”[37] thus limiting the protection to just the elimination of the negligence penalty.

Furthermore, the news release states that, “[r]ulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents.”[38] This too comes with a slight caveat as the IRS clarifies that, “[i]n applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings and procedures must be considered.”[39]

Unfortunately, the news release does not address whether taxpayers and advisors may rely on the IRS’s own Publications, tax form instructions, and other material posted on the IRS website, so readers beware!

9. Other Rollover Traps. When a Plan Participant takes a 60-day rollover, the income is shown on the Form 1040 income tax return and can detrimentally impact scholarship qualification, even when the entire amount withdrawn is rolled over. This problem should not occur when there is a transfer directly from a Qualified Retirement Plan to an IRA in normal fashion.

10. Designated Beneficiary. An individual beneficiary of an IRA/Plan, or a beneficiary of a trust named as the beneficiary of an IRA/Plan distributions whose status is used to determine if such beneficiary is an Eligible Designated Beneficiary, and whether

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[36] *IRS Updates Process For Frequently Asked Questions On New Tax Legislation and Addresses Reliance Concerns*, I.R.S. (Oct. 15, 2021), https://www.irs.gov/newsroom/irs-updates-process-for-frequently-asked-questions-on-new-tax-legislation-and-addresses-reliance-concerns.

[37] *Id.*

[38] *Id.*

[39] *Id.*

the 10-Year Rule will apply, or if life expectancy of the Eligible Designated Beneficiary will be used for purposes of determining the Required Minimum Distributions.

Note - As discussed below, for a Conduit Trust (which must pay all IRA/Plan withdrawals to the Designated Beneficiary), older individuals and other entities that are beneficiaries of the Trust can be ignored. For an Accumulation Trust, the Designated Beneficiary must be the oldest named possible individual Tier I or Tier II Beneficiary of the trust to which the IRA/Plan is payable, and there can be no non-person beneficiaries as Tier I or Tier II Beneficiaries under the Accumulation Trust as of September 30th of the calendar year after the death of the Plan Participant.

11. Eligible Designated Beneficiary. The five categories of beneficiaries that are eligible for the Life Expectancy Rule under the SECURE Act for Plan Participants who die after 2019 are as follows:

    (a) The Surviving Spouse;

    (b) A minor child, as defined in Chapter 7, Paragraph 11(b);

    (c) A disabled beneficiary, as defined in Chapter 7, Paragraph 11(c);

    (d) A chronically ill beneficiary, as defined in Chapter 7, Paragraph 11(d); or

    (e) An individual not more than ten years younger than the deceased Plan Participant.

12. 10-Year Rule. The 10-Year Rule is now available as the method of withdrawal in many scenarios. For Plan Participants who die prior to their Required Beginning Date (generally April 1st of the calendar year following the calendar year in which the Plan Participant reaches the age of 72), the 10-Year Rule is very similar to the pre-SECURE Act 5-Year Rule, except that all benefits must be paid out of the IRA/Plan on or before December 31st of the 10th calendar year that follows the applicable triggering event, so that the 10-year period will run less than eleven years after the triggering event.

    For example, if a Plan Participant dies on September 30, 2021 at the age of 65 (prior to his or her Required Beginning Date), and the beneficiary is subject to the 10-Year Rule, then distributions do not have to be made until ten years and three months later on December 31, 2031.

    As further discussed in Chapter 8, the February 2022 Proposed Regulations provide that, if the Plan Participant dies after his or her Required Beginning Date then distributions begin on the first calendar year following the year of the Plan Participant's death based on the life expectancy of the Designated Beneficiary, and each year thereafter until all assets in the IRA/Plan must be distributed to the applicable beneficiary(ies) by the end of the 10th year following the calendar year of the Plan Participant's death.

In other words, there will be Required Minimum Distributions based on the age of the Designated Beneficiary (or the Plan Participant if the Plan Participant was over the Required Beginning Date on death) of the IRA/Plan in years 1 through 9, following by a complete liquidation of the IRA/Plan in year 10.

For example, if a Plan Participant dies on September 30, 2022 after reaching his or her Required Beginning Date, and the payments are subject to the 10-Year Rule, then the beneficiary must take annual Required Minimum Distributions in each of the nine years following the year of the Plan Participant's death based upon what would have applied under the pre-SECURE Act rules, and all assets of the IRA/Plan must be distributed by December 31, 2032.

The start date for the 10-Year Rule will apply based upon December 31st of the year in which one of the following triggering events occurs:

(a) The death of a Plan Participant;

(b) The death of a Surviving Spouse who rolled over the inherited IRA/Plan into his or her IRA;

(c) The death of a beneficiary of an inherited IRA/Plan, which was inherited after the death of Plan Participant who died before January 1, 2020;

(d) When a minor beneficiary who is the child of the deceased Plan Participant and who is the Designated Beneficiary of the IRA/Plan is considered to have reached age 21 (or has died); or

(e) The death of an Eligible Designated Beneficiary who is the Designated Beneficiary of the IRA/Plan.

It makes sense to withdraw any remaining amounts early in the applicable 10th year, so that post withdrawal growth in value and qualified dividends will not be taxed at ordinary rates, which would otherwise apply if and when such remaining amounts are withdrawn late in December of such year.

13. Life Expectancy Rule. The rule which permits the "stretch" of Required Minimum Distributions from an IRA/Plan over a beneficiary's or the Participant's life expectancy after the Participant's death is known as the "Life Expectancy Rule." This Rule was the foundation for the "Stretch IRA" planning techniques which allowed for the deferral of distributions from an inherited IRA/Plan (and deferral of the corresponding income tax burden associated with such distributions) over many years, and has been largely abrogated unless an IRA/Plan is left to an Eligible Designated Beneficiary under certain circumstances.

14. At-Least-As-Rapidly Rule. Where a Plan Participant dies after reaching his or her Required Beginning Date, Required Minimum Distributions may have to come out of the IRA/Plan "at least as rapidly" as they would have if the Plan Participant were still living. For example, where no Designated Beneficiary exists, Required Minimum Distributions can be made according to the remaining life expectancy of the deceased Plan Participant, notwithstanding whether the beneficiary is an individual, but only if the Plan Participant dies after the Required Beginning Date.

    Prior to the SECURE Act, it was clear under the present Treasury Regulations that when the Plan Participant died after reaching his or her Required Beginning Date, a beneficiary would have the benefit of the longer of (1) the Applicable Payment Mode associated with the deceased Plan Participant's life expectancy; or (2) the Applicable Payment Mode that would otherwise apply, even where there was a Designated Beneficiary. Thus, the "At-Least-As-Rapidly Rule" method could be used when the Plan Participant has a longer life expectancy than the Designated Beneficiary in order for a longer distribution period to apply.

15. Designation Date. The Designation Date is September 30th of the calendar year following the year of death of the Plan Participant. This is the date on which the Designated Beneficiary is determined for the purposes of calculating the Applicable Payment Mode of the Required Minimum Distributions. As stated above, it is often advisable to remove or eliminate one or more beneficiaries after the death of a Plan Participant, but before the Designation Date. See Illustration 2.11 below for a summary of important dates after the Death of the Plan Participant.

    The Designation Date has even more importance under the 2022 Proposed Regulations as discussed in Chapter 8.

16. Administrator. The IRA sponsor or Qualified Retirement Plan administrator, or comparable person or entity. For a pension or 401(k) plan, this will typically be someone who works for the sponsoring company who administers the plan. For an IRA, this will typically be the company that sponsors it, such as Charles Schwab, Wells Fargo, Vanguard, or a bank or credit union.

17. IRA Custodian. A company or bank that sponsors an IRA account, such as Merrill Lynch, Vanguard, or Wells Fargo.

    Note - Many sponsors will not permit an inherited IRA to be distributed intact to a trust that receives the IRA on the death of the Plan Participant, so custodians/brokers/banks may have to be changed after the Plan Participant dies. These sponsors will sometimes only be willing to have inherited IRAs, or portions thereof, payable to a trust only after the receipt of a court order and/or an IRS Private Letter Ruling.

18. IRA Trustee. A bank with trust company powers, or a nonbank trust company that has been approved by the IRS under Treasury Regulation 1.408-2(e), to serve as a trustee/custodian under the rules that permit trusteed IRA arrangements. These

rules permit the same customized trust agreement that is entered into with the trustee to also control disposition and payment rights to avoid having to program these into the Plan Participant's will and/or living trust system, but the same rules with respect to Required Minimum Distributions (e.g., the requirements with respect to the determination of the Designated Beneficiary of the Trust) will still apply.

19. Individual Retirement Trust ("IRT"). The Individual Retirement Trust arrangement is permitted under Internal Revenue Code Section 408(a) and known as an "Individual Retirement Trust" or "IRT." An Individual Retirement Trust is very similar to a typical IRA custodianship arrangement because a trust company holds the trust assets to comply with the IRA administration rules. Unlike a typical IRA custodianship arrangement where the beneficiary may be an individual, a Conduit Trust, or an Accumulation Trust, an Individual Retirement Trust can in effect become a Conduit Trust or an Accumulation Trust without the need of extraneous trust documents or provisions under a Last Will and Testament or a Revocable Living Trust which provides for one or more separate irrevocable trusts to arise upon the death of the Testator/Living Trust Settlor in order to qualify.

    In other words, instead of having a traditional IRA that would be payable to a trust on death, and then having the trustee receive Required Minimum Distributions each year that in turn can be accumulated, paid out to the beneficiary, or paid to third parties to hold and use for the beneficiary, an Individual Retirement Trust avoids the need for an intermediary Accumulation Trust or Conduit Trust.

    For example, the Individual Retirement Trust could include language such as: "After my death, the trustee shall hold the individual retirement trust for my son, John, paying him only such amounts as needed for his health, education, maintenance, and support, after taking into account other sources of income and resources available to him."

    Individual Retirement Trusts do have some disadvantages which can include the requirement to pay Trustee fees that can exceed typical IRA costs and the inability to transfer the account to another IRA provider after the owner's death, depending upon the provider's policies.

    See Edwin Morrow's article "Trusteed IRAs: An Elegant Estate Planning Option", Trusts and Estates, Sept 2009 for an excellent discussion on Individual Retirement Trusts.

20. Qualified Annuity. An annuity contract issued by an insurance carrier using IRA/Plan monies which qualifies as an IRA/Plan and therefore follows the IRA/Plan rules set forth herein as opposed to the "non-qualified annuity" rules under Internal Revenue Code Section 72. IRA rules will apply here, but flexibility may be significantly limited by the annuity contract and policies of the carrier.

21. <u>Charitable Gift Annuity</u>. An arrangement whereby a charity receives a contribution of cash or appreciated assets and agrees to pay a lifetime annuity to the donor or another person or persons. The excess of the value of the amounts given to charity over the initial present value of the right to receive payments under the annuity contract will constitute a charitable contribution by the donor. IRA/Plan made payable to charity in exchange for annuity to be paid based upon the life of designated individuals will be more common under the SECURE Act.

22. <u>Applicable Payment Mode</u>. The method of payment of Required Minimum Distributions, as described in Chapter 4 - Payout Methods, which will apply after the death of the Plan Participant and will usually continue after the death of the Designated Beneficiary of the Plan Participant's IRA/Plan.

23. <u>Applicable Life Expectancy Table</u>. The Life Expectancy Tables published by the IRS, which apply numbers based on the Applicable Payment Mode of Required Minimum Distributions after the Plan Participant reaches his or her Required Beginning Date, or after the death of the Plan Participant. There are three Life Expectancy Tables: The Single Life Table, the Uniform Life Table, and the Joint/Survivor Table.

24. <u>Applicable Divisor</u>. The divisor for the year in question under the Applicable Life Expectancy Table which is used to determine the amount of the Required Minimum Distribution for a given year. The value of the IRA/Plan on December 31 of the prior calendar year is divided by the divisor in order to determine the amount of the Required Minimum Distribution for the given year.

25. <u>Recalculation of Life Expectancy</u>. A method of calculation whereby the Person's life expectancy is determined each year from the Applicable Life Expectancy Table, which takes into account that every year a person's life expectancy is reduced by less than one year. This rule will apply during the lifetime of the Plan Participant, and during the lifetime of a Surviving Spouse beneficiary who is able to follow the rollover rules. The Applicable Payment Mode is determined by looking at the age of the Plan Participant or the Plan Participant's Spouse (as applicable) on the Applicable Life Expectancy Table for each year in which a Required Minimum Distribution must be made. The life expectancy of the Plan Participant or the Plan Participant's Spouse is therefore "recalculated" each year.

    For example, if an unmarried Plan Participant turns age 72 during Year 1, then she would look at the row under the Uniform Lifetime Table that corresponds to age 72 in order to determine the Applicable Divisor (27.4). In the next year, when the Plan Participant turns age 73, she will look at the row under the Uniform Lifetime Table that corresponds to age 73 to determine the Applicable Divisor (26.5).

    If a Person other than the Plan Participant's Spouse is a beneficiary of the IRA/Plan, or if the Plan Participant's Spouse is a beneficiary of the IRA/Plan but is not the sole or Designated Beneficiary of the IRA/Plan, then the Recalculation of Life Expectancy principle will not apply. Instead, for Eligible Designated Beneficiaries, the Applicable Divisor for the first calendar year after the year of the Plan Participant's death is determined by looking at the row under the Single Life Table that corresponds to the oldest age of the Designated Beneficiary in such calendar year, and the Applicable Divisor is determined for all subsequent years by subtracting one from the Applicable Divisor of the preceding calendar year. For all other Designated Beneficiaries, the 10-Year Rule will apply.

For example, if the Designated Beneficiary is a chronically ill beneficiary (or is an individual Designated Beneficiary prior to January 1, 2020) and is age 72 in the calendar year after the year of the Plan Participant's death, then the Applicable Divisor for such year is 17.2. For the next calendar year, when the Designated Beneficiary is age 73, the Applicable Divisor is 16.2, and for each subsequent year, the Applicable Divisor for the preceding year is subtracted by one, and will therefore be 15.2 years, rather than re-determining life expectancy each year by "recalculation."

The following chart illustrates the effect of each of the four calculation methods that are available for plans where the Plan Participant died before January 1, 2020, and the significant difference between the results that apply under each method where the beneficiary of an IRA is age 70 in the first year of withdrawal (as original owner, or beneficiary where original owner died before reaching the Required Beginning Date).

NOTE: All Life Expectancy charts in this Book have been updated for new IRA Life Expectancy Tables that began to apply in 2021. These new tables increased the life expectancy assumptions and thus reduced the Required Minimum Distributions from an IRA or rollover IRA based upon the Uniform Life Table as follows:[40]

LIFE EXPECTANCY BASED ON THE UNIFORM LIFE TABLE

Age of IRA Owner	Pre-2021 Distribution Percentage	Post-2020 Distribution Percentage
72	3.91	3.67
75	4.37	4.07
80	5.35	4.95
85	6.76	6.25
90	8.75	8.27
95	11.63	11.24
100	15.88	15.71

[40] Our thanks to Robert Keebler and Christopher Hoyt for providing these numbers in their presentation entitled *The SECURE ACT and the Charitable Remainder Trust - A Deep Dive.*

ILLUSTRATION 2.1 – MINIMUM DISTRIBUTION RULE CALCULATION PRIOR TO JANUARY 1, 2020

Illustration 2.1 demonstrates Minimum Distribution Rule Calculation prior to January 1, 2020 for an individual who begins receiving distributions at age 70 or a Designated Beneficiary where distributions begin at age 70. Also displayed in percentages based off the applicable divisor (% = 1 ÷ divisor).[41]

Age	Likelihood of Having Died, Starting at Age 70	Participant Married to Spouse More than 10 Years Younger (Using the "Joint and Survivor Table" with a Spouse 15 years Younger than the Participant)	Participant Is Treated as if Married to a Spouse 10 Years Younger (whether married or not) (Using the "Uniform Lifetime Table")	Individual Designated Beneficiary with Recalculation of Life Expectancy (Using the "Single Life Table," Recalculated Annually)	Individual Designated Beneficiary with No Recalculation of Life Expectancy (Using the "Single Life Table," Not Recalculated Annually)
70	0.5%	31.1 / 3.21%	27.4 / 3.65%	17.0 / 5.88%	17.0 / 5.88%
71	1.2%	30.1 / 3.32%	26.5 / 3.77%	16.3 / 6.13%	16.0 / 6.25%
72	2.3%	29.2 / 3.42%	25.6 / 3.91%	15.5 / 6.45%	15.0 / 6.67%
73	3.6%	28.3 / 3.53%	24.7 / 4.05%	14.8 / 6.76%	14.0 / 7.14%
74	5.1%	27.4 / 3.65%	23.8 / 4.20%	14.1 / 7.09%	13.0 / 7.69%
75	7.0%	26.5 / 3.77%	22.9 / 4.37%	13.4 / 7.46%	12.0 / 8.33%
76	9.1%	25.6 / 3.91%	22.0 / 4.55%	12.7 / 7.87%	11.0 / 9.09%
77	11.5%	24.7 / 4.05%	21.2 / 4.72%	12.1 / 8.26%	10.0 / 10.00%
78	14.3%	23.8 / 4.20%	20.3 / 4.93%	11.4 / 8.77%	9.0 / 11.11%
79	17.6%	22.9 / 4.37%	19.5 / 5.13%	10.8 / 9.26%	8.0 / 12.50%
80	21.4%	22.1 / 4.52%	18.7 / 5.35%	10.2 / 9.80%	7.0 / 14.29%
81	25.7%	21.2 / 4.72%	17.9 / 5.59%	9.7 / 10.31%	6.0 / 16.66%
82	30.5%	20.4 / 4.90%	17.1 / 5.85%	9.1 / 10.99%	5.0 / 20.00%
83	35.9%	19.5 / 5.13%	16.3 / 6.13%	8.6 / 11.62%	4.0 / 25.00%
84	41.6%	18.7 / 5.35%	15.5 / 6.45%	8.1 / 12.35%	3.0 / 33.33%
85	47.5%	17.9 / 5.59%	14.8 / 6.76%	7.6 / 13.16%	2.0 / 50.00%
86	53.3%	17.1 / 5.85%	14.1 / 7.09%	7.1 / 14.08%	1.0 / 100.00%
87	59.0%	16.4 / 6.10%	13.4 / 7.46%	6.7 / 14.93%	N/A
88	64.6%	15.6 / 6.41%	12.7 / 7.87%	6.3 / 15.87%	N/A
89	70.1%	14.9 / 6.71%	12.0 / 8.33%	5.9 / 16.95%	N/A
90	75.1%	14.2 / 7.04%	11.4 / 8.77%	5.5 / 18.18%	N/A
91	79.7%	13.5 / 7.41%	10.8 / 9.26%	5.2 / 19.23%	N/A
92	83.8%	12.8 / 7.81%	10.2 / 9.80%	4.9 / 20.41%	N/A
93	87.3%	12.1 / 8.26%	9.6 / 10.42%	4.6 / 21.74%	N/A
94	90.3%	11.5 / 8.70%	9.1 / 10.99%	4.3 / 22.26%	N/A
95	92.7%	10.9 / 9.17%	8.6 / 11.63%	4.1 / 24.39%	N/A
96	94.6%	10.3 / 9.71%	8.1 / 12.35%	3.8 / 26.32%	N/A
97	96.1%	9.7 / 10.31%	7.6 / 13.16%	3.6 / 27.78%	N/A
98	97.3%	9.2 / 10.87%	7.1 / 14.08%	3.4 / 29.41%	N/A

[41] The numbers will be updated when the next edition of the book is released, which will be shortly after the Proposed Regulations are finalized.

Age	Likelihood of Having Died, Starting at Age 70	Participant Married to Spouse More than 10 Years Younger (Using the "Joint and Survivor Table" with a Spouse 15 years Younger than the Participant)	Participant Is Treated as if Married to a Spouse 10 Years Younger (whether married or not) (Using the "Uniform Lifetime Table")	Individual Designated Beneficiary with Recalculation of Life Expectancy (Using the "Single Life Table," Recalculated Annually)	Individual Designated Beneficiary with No Recalculation of Life Expectancy (Using the "Single Life Table," Not Recalculated Annually)
99	98.1%	8.6 / 11.63%	6.7 / 14.93%	3.1 / 32.26%	N/A
100	98.7%	8.1 / 12.35%	6.3 / 15.87%	2.9 / 34.48%	N/A

JOINT AND LAST SURVIVOR TABLE

TABLE II (continued)
(Joint Life and Last Survivor Expectancy)
For Use by Owners Whose Spouses Are More Than 10 Years Younger and Are the Sole Beneficiaries of Their IRA/Plans

AGES	60	61	62	63	64	65	66	67	68	69
76	26.3	25.6	24.8	24.1	23.4	22.7	22.0	21.4	20.8	20.2
77	26.2	25.4	24.7	23.9	23.2	22.5	21.8	21.2	20.6	19.9
78	26.1	25.3	24.6	23.8	23.1	22.4	21.7	21.0	20.3	19.7
79	26.0	25.2	24.4	23.7	22.9	22.2	21.5	20.8	20.1	19.5
80	25.9	25.1	24.3	23.6	22.8	22.1	21.3	20.6	20.0	19.3
81	25.8	25.0	24.2	23.4	22.7	21.9	21.2	20.5	19.8	19.1
82	25.8	24.9	24.1	23.4	22.6	21.8	21.1	20.4	19.7	19.0
83	25.7	24.9	24.1	23.3	22.5	21.7	21.0	20.2	19.5	18.8
84	25.6	24.8	24.0	23.2	22.4	21.6	20.9	20.1	19.4	18.7
85	25.6	24.8	23.9	23.1	22.3	21.6	20.8	20.1	19.3	18.6
86	25.5	24.7	23.9	23.1	22.3	21.5	20.7	20.0	19.2	18.5
87	25.5	24.7	23.8	23.0	22.2	21.4	20.7	19.9	19.2	18.4
88	25.5	24.6	23.8	23.0	22.2	21.4	20.6	19.8	19.1	18.3
89	25.4	24.6	23.8	22.9	22.1	21.3	20.5	19.8	19.0	18.3
90	25.4	24.6	23.7	22.9	22.1	21.3	20.5	19.7	19.0	18.2
91	25.4	24.5	23.7	22.9	22.1	21.2	20.5	19.7	18.9	18.2
92	25.4	24.5	23.7	22.9	22.0	21.2	20.4	19.6	18.9	18.1
93	25.4	24.5	23.7	22.8	22.0	21.2	20.4	19.6	18.8	18.1
94	25.4	24.5	23.6	22.8	22.0	21.1	20.4	19.6	18.8	18.0
95	25.3	24.5	23.6	22.8	22.0	21.1	20.3	19.6	18.8	18.0
96	25.3	24.5	23.6	22.8	21.9	21.1	20.3	19.5	18.8	18.0
97	25.3	24.5	23.6	22.8	21.9	21.1	20.3	19.5	18.8	18.0
98	25.3	24.4	23.6	22.8	21.9	21.1	20.3	19.5	18.7	17.9
99	25.3	24.4	23.6	22.7	21.9	21.1	20.3	19.5	18.7	17.9
100	25.3	24.4	23.6	22.7	21.9	21.1	20.3	19.5	18.7	17.9
101	25.3	24.4	23.6	22.7	21.9	21.1	20.2	19.4	18.7	17.9
102	25.3	24.4	23.6	22.7	21.9	21.0	20.2	19.4	18.7	17.9
103	25.3	24.4	23.6	22.7	21.9	21.0	20.2	19.4	18.6	17.9
104	25.3	24.4	23.5	22.7	21.9	21.0	20.2	19.4	18.6	17.8

TABLE II (continued) (Joint Life and Last Survivor Expectancy) For Use by Owners Whose Spouses Are More Than 10 Years Younger and Are the Sole Beneficiaries of Their IRA/Plans										
AGES	**60**	**61**	**62**	**63**	**64**	**65**	**66**	**67**	**68**	**69**
105	25.3	24.4	23.5	22.7	21.9	21.0	20.2	19.4	18.6	17.8
106	25.3	24.4	23.5	22.7	21.9	21.0	20.2	19.4	18.6	17.8
107	25.2	24.4	23.5	22.7	21.8	21.0	20.2	19.4	18.6	17.8
108	25.2	24.4	23.5	22.7	21.8	21.0	20.2	19.4	18.6	17.8
109	25.2	24.4	23.5	22.7	21.8	21.0	20.2	19.4	18.6	17.8
110	25.2	24.4	23.5	22.7	21.8	21.0	20.2	19.4	18.6	17.8
111	25.2	24.4	23.5	22.7	21.8	21.0	20.2	19.4	18.6	17.8
112	25.2	24.4	23.5	22.7	21.8	21.0	20.2	19.4	18.6	17.8
113	25.2	24.4	23.5	22.7	21.8	21.0	20.2	19.4	18.6	17.8
114	25.2	24.4	23.5	22.7	21.8	21.0	20.2	19.4	18.6	17.8
115+	25.2	24.4	23.5	22.7	21.8	21.0	20.2	19.4	18.6	17.8

Example:

An 80-year old Participant is married to a spouse age 61. The Applicable Divisor under this example is equal to 25.1 years. The Required Minimum Distribution for the year would equal 3.98% (1 ÷ 25.1) of the account balance.

The following year, the Applicable Divisor would be recalculated. The Applicable Divisor would now be 24.2 years, and the Required Minimum Distribution would equal 4.13% (1 ÷ 24.2) of the account balance.

In Year 3, the Applicable Divisor would be 23.4, and the Required Minimum Distribution would equal 4.27% (1 ÷ 23.4) of the account balance.

The Applicable Divisor is recalculated for each subsequent year to calculate the Required Minimum Distribution.

UNIFORM LIFETIME TABLE

TABLE III
(Uniform Lifetime)

For Use by:

- Unmarried Owners;
- Married Owners Whose Spouses Are Not More Than 10 Years Younger; and
- Married Owners Whose Spouses Are Not the Sole Beneficiaries of Their IRAs

Age	Distribution Period	Age	Distribution Period
70	27.4	93	96.6
71	26.5	94	9.1
72	25.6	95	8.6
73	24.7	96	8.1
74	23.8	97	7.6
75	22.9	98	7.1
76	22.0	99	6.7
77	21.2	100	6.3
78	20.3	101	5.9
79	19.5	102	5.5
80	18.7	103	5.2
81	17.9	104	4.9
82	17.1	105	4.5
83	16.3	106	4.2
84	15.5	107	3.9
85	14.8	108	3.7
86	14.1	109	3.4
87	13.4	110	3.1
88	12.7	111	2.9
89	12.0	112	2.6
90	11.4	113	2.4
91	10.8	114	2.1
92	10.2	115 and over	1.9

Example:

A 70-year-old Participant's Applicable Divisor is 27.4 years. The Required Minimum Distribution for the year would equal 3.65% (1 ÷ 27.4) of the account balance.

The following year, the Applicable Divisor would be recalculated. The Applicable Divisor would now be 26.5 years, and the Required Minimum Distribution would equal 3.77% (1 ÷ 26.5) of the account balance.

In Year 3, Applicable Divisor period would be 25.6, and the Required Minimum Distribution would equal 3.91% (1 ÷ 25.6) of the account balance.

The Applicable Divisor is recalculated for each subsequent year to calculate the Required Minimum Distribution.

SINGLE LIFE TABLE

TABLE I
(Single Life Expectancy)

For Use by:
- Eligible Designated Beneficiaries who are the sole beneficiaries of an IRA/Plan; or
- All individual beneficiaries of an IRA/Plan that was inherited prior to January 1, 2020

AGE	Life	Age	Life Expectancy
0	82.4	28	55.3
1	81.6	29	54.3
2	80.6	30	53.3
3	79.7	31	52.4
4	78.7	32	51.4
5	77.7	33	50.4
6	76.7	34	49.4
7	75.8	35	48.5
8	74.8	36	47.5
9	73.8	37	46.5
10	72.8	38	45.6
11	71.8	39	44.6
12	70.8	40	43.6
13	69.9	41	42.7
14	68.9	42	41.7
15	67.9	43	40.7
16	66.9	44	39.8
17	66.0	45	38.8
18	65.0	46	37.9
19	64.0	47	37.0
20	63.0	48	36.0
21	62.1	49	35.1
22	61.1	50	34.2
23	60.1	51	33.3
24	59.1	52	32.3
25	58.2	53	31.4
26	57.2	54	30.5
27	56.2	55	29.6

Example:

A 35- year-old is a beneficiary of his father's IRA who died prior to January 1, 2020. His Applicable Divisor is 48.5 years. The Required Minimum Distribution for the year would equal 2.06% (1 ÷ 48.5) of the account balance.

The following year, Applicable Divisor is NOT recalculated, instead the period is reduced by one to 47.5 years. The Required Minimum Distribution would equal 2.11% (1 ÷ 47.5) of the account balance.

In Year 3, the Applicable Divisor would be 46.5 and the Required Minimum Distribution would equal 2.15% (1 ÷ 46.5) of the account balance. The Applicable Divisor is never recalculated and will be reduced by one each subsequent year to calculate the Required Minimum Distributions.

If the beneficiary's father died on or after January 1, 2020, then the 10-Year Rule would apply as discussed in more detail in Chapter 7.

26. <u>See-Through Trusts, Accumulation Trusts, and Conduit Trusts</u>. As described in subsequent chapters, certain trusts can receive IRA/Plan benefits when the Plan Participant has died prior to January 1, 2020 without triggering the "5-Year Rule" or the "At-Least-As-Rapidly Rule," and instead allowing the more favorable 10-Year Rule or Life Expectancy Rule to apply. If the Plan Participant has died on or after January 1, 2020, then the Life Expectancy Rule has been replaced with a 10-Year Rule unless the IRA/Plan is made payable to an Eligible Designated Beneficiary or a See-Through Trust for the benefit of an Eligible Designated Beneficiary. The rules that apply on or after January 1, 2020 are discussed extensively in Chapter 7. An Accumulation Trust can retain distributions from the IRA/Plan whereby a Conduit Trust must pay all distributions received directly from the IRA/Plan to a Designated Beneficiary without delay. The term "See-Through Trust" refers to both Accumulation Trusts and Conduit Trusts.

27. <u>5-Year Rule (or the 5th year After Death Method)</u>. The Required Minimum Distribution rule that requires benefits to be paid out by December 31st of the 5th calendar year following the death of a Plan Participant who has not reached Required Beginning Date (April 1st of the year in which he or she reaches the age of 72 after January 1, 2020 [or 70½ prior to January 1, 2020]), will apply if there is not a more favorable method of Required Minimum Distributions that will apply. If the Plan Participant dies after Required Beginning Date, then the 5-Year Rule cannot be used and instead the life expectancy of the deceased Plan Participant will continue to be used under the "At-Least-As-Rapidly Rule."

    The CARES Act modified the 5-Year Rule for situations where a Plan Participant dies after 2014 but before 2020, if the date of death is before his or her Required Beginning Date. In such case, the 5-Year Rule effectively becomes a "6-Year Rule" because the calendar year 2020 is not taken into account.

    For example, if a Plan Participant dies on April 2, 2016 prior to her Required Beginning Date, and the 5-Year-Rule applies with respect to the Required Minimum Distributions from her IRA, then, as a result of the CARES Act, all assets must be distributed no later than December 31, 2022 (not by December 31, 2021, which would be the deadline but for the CARES Act).

    As another example, if a Plan Participant dies in 2021 before reaching age 72, and his IRA/Plan is left to his estate, then all assets must be distributed from the IRA/Plan by December 31, 2026, although no distributions will be required whatsoever before such deadline. This may be more advantageous for older Designated Beneficiaries.

For example, if the life expectancy of the Designated Beneficiary is only 4.6 years because he or she is age 93, then the choices for distribution can be seen in Illustration 2.2 below:[42]

ILLUSTRATION 2.2 - LIFE EXPECTANCY METHOD VS. FIVE YEAR ALTERNATIVE

(Illustrated for a 93-Year-Old with $100,000 IRA Balance, assuming a 5% Rate of Return)

Life Expectancy Method (Required Minimum Distributions using Uniform Lifetime Table)							
Year	**Age**	**IRA Account Balance**	**Growth at 5%**	**Required Minimum Distribution %**	**Required Minimum Distribution**	**Year End IRA Account Balance**	**Ending Account Balance Plus**
1	93	$100,000.00	$5,000.00	21.74%	$(22,827.00)	$82,173.00	$105,00
2	94	$82,173.00	$4,108.65	27.78%	$(23,969.04)	$62,312.61	$109,10
3	95	$62,312.61	$3,115.63	38.46%	$(25,163.70)	$40,264.54	$112,22
4	96	$40,264.54	$2,013.23	62.50%	$(26,423.60)	$15,854.16	$114,23
5	97	$15,854.16	$792.71	100.00%	$(16,646.97)	$-	$115,03

Five-Year Rule Alternative (Account balance must be distributed within five years)								
Year	**Age**	**IRA Account Balance**	**Growth at 5%**	**Required Minimum Distribution %**	**Required Minimum Distribution**	**Year End IRA Account Balance**	**Ending Account Balance Plus Cumulative Distributions**	**Potential Benefit of Using the Five-Year Alternative**
1	93	$100,000.00	$5,000.00	0.00%	$-	$105000.00	$105,000.00	$-
2	94	$105,000.00	$5,250.00	0.00%	$-	$110250.00	$110,250.00	$1,141.35
3	95	$110,250.00	$5,512.50	0.00%	$-	$115762.50	$115,762.50	$3,538.22
4	96	$115,762.50	$5,788.13	0.00%	$-	$121550.63	$121,550.63	$7,313.22
5	97	$121,550.63	$6,077.53	100.00%	$(127,628.16)	$-	$127,628.16	$12,597.94

28. <u>Trust Protector</u>. An individual and/or entity given the power to make changes to trust agreement provisions.

29. <u>Toggle</u>. To, in effect, pull a switch that causes changes in a trust document to facilitate tax or other planning. Many trust documents have language that permits fiduciaries, or Trust Protectors acting in a non-fiduciary capacity, to change what would have been an Accumulation Trust into a Conduit Trust before the Designation Date (September 30th following the calendar year of death of the Plan Participant). See Chapter 3, Section IV.

30. <u>Natalie Choate's Abbreviations</u>. Natalie Choate's book, "*Life and Death Planning for Retirement Benefits,*" is an indispensable guide and the standard of practice for

[42] Note that the above numbers are not updated to account for changes in the mortality tables that have occurred since 2020. The tables also do not account for changes that would be made by the Proposed Regulations released in 2022. The tables will be updated when the Final Regulations are released.

anyone giving advice in this area. The book can be ordered by going to https://www.ataxplan.com/life-and-death-planning-for-retirement-benefits/. We strongly recommend that readers also take a look at what else is available from Natalie's website. We thank Natalie Choate for her excellent writing in this area. She is without a doubt the most dynamic and constructive force that has occurred in any one area of estate and tax planning law for our generation of planners. We also thank Jonathan Blattmachr and Michael Graham for making Natalie's excellent book available in electronic form on the Interactive Legal platform.

Natalie Choate uses a number of abbreviations, which are as follows:

ADP	Applicable Distribution Period
AGI	Adjusted Gross Income
CODA	Cash-or-Deferred Arrangement
COLA	Cost-of-Living Adjustment
CODE	Internal Revenue Code of 1986
DB	Designated Beneficiary
DNI	Distributable Net Income
DOL	Department of Labor
DQP	Disqualified Person
ERISA	Employee Retirement Income Security Act of 1974
IRD	Income in Respect of a Decedent
IRS	Internal Revenue Service
IRT	Individual Retirement Trust (trusteed IRA)
MAGI	Modified Adjusted Gross Income
MRD	Minimum Required Distribution
PLR	IRS Private Letter Ruling
PPA '06	The Pension Protection Act of 2006
Prop. Reg	Proposed Treasury Regulation
PT	Prohibited Transaction
QRP	Qualified Retirement Plan
RBD	Required Beginning Date
REA	Retirement Equity Act of 1984
UBTI	Unrelated Business Taxable Income

II. Crucial Rules

1. 10% Excise Tax. A Plan Participant who has not reached age 59½ will pay a 10% excise tax on taxable distributions (in addition to the normal income tax), unless one of the exceptions from Internal Revenue Code Section 72(t)(2) applies, which are described in greater detail on Page 22 above, or the Coronavirus-Related Distribution exception applies. Certain exceptions are only applicable in limited situations, as discussed in Chapter 1, Section II (B).

2. Coronavirus-Related Distribution. In response to the COVID-19 pandemic, the CARES Act was enacted on March 27, 2020, which provides relief to certain taxpayers who withdraw up to $100,000 of assets from an IRA/Plan before attaining the age of 59 1/2. Specifically, the CARES Act eliminates the 10% excise tax for

withdrawals of up to $100,000 in 2020 made by a Plan Participant (or by a Surviving Spouse who inherited an IRA/Plan from a deceased Plan Participant and did not roll over such Plan Participant's IRA/Plan into his or her own) from an IRA/Plan before such Plan Participant or Surviving Spouse reaches the age of 59 ½ if such Plan Participant or Surviving Spouse is a "Qualified Individual" by satisfying one or more of the following:

(a) he or she is diagnosed with the virus SARS-CoV-2 or the disease COVID-19 by a test approved by the Centers for Disease Control and Prevention (CDC);

(b) he or she has a spouse or dependent who is diagnosed with the virus or disease by such a test; or

(c) he or she (or his or her spouse, or someone who shares his or her principal residence) experiences adverse financial consequences as a result of:

  (i) being quarantined;

  (ii) being furloughed or laid off or having work hours reduced due to such virus or disease;

  (iii) being unable to work due to lack of childcare due to such virus or disease;

  (iv) closing or reducing hours of a business owned or operated by the individual (or the individual's spouse, or someone who shares his or her principal residence) due to such virus or disease;

  (v) having a reduction in pay (or self-employment income) due to COVID-19 or having a job offer extended or a start date for a job delayed due to COVID-19; or

  (vi) other factors as determined by the Secretary of the Treasury (or the Secretary's delegate).

Such a Distribution is called a "Coronavirus-Related Distribution." The taxpayer can decide whether to (1) treat the Distribution as an interest-free loan by making a contribution to the applicable IRA/Plan no later than three years after the date of the Distribution (in which case, the Distribution and subsequent contribution are treated as an eligible rollover distribution that is rolled over within 60 days of the Distribution); (2) pay income tax on the entire Distribution for the year in which it is made, in same manner that applies to Required Minimum Distributions and other distributions from the IRA/Plan; or (3) pay income tax on the distribution one-third each over three tax years (the year of the Distribution, and the following two years). Regardless of which alternative is selected, the 10% excise tax does not apply, despite the taxpayer otherwise not being eligible to take a distribution from the IRA/Plan.

The CARES Act eliminated the requirement that Required Minimum Distributions be made in the calendar year 2020. Therefore, no Required Minimum Distributions are required to be made in 2020, although this does not eliminate the requirement that Required Minimum Distributions be made in future years (or years prior to 2020).

3. Required Minimum Distributions ("RMDs"). The amounts which must be paid out in a given year under the Applicable Payment Mode, based upon the life expectancy of the Plan Participant or Eligible Designated Beneficiary, or amounts that must be paid under another applicable payment method. The Applicable Payment Mode also depends upon whether the IRA/Plan names the Plan Participant's Surviving Spouse as the sole beneficiary of the IRA/ Plan after the death of the Plan Participant. The majority of different types of IRA/Plans cannot be aggregated together to satisfy the Required Minimum Distribution Rules. Below (Illustration 2.3) is a chart that summarizes the aggregation rules for Required Minimum Distributions.

ILLUSTRATION 2.3 – AGGREGATION RULES FOR DISTRIBUTIONS

	Aggregation Rules for Distributions
1	Each Qualified Retirement Plan must be withdrawn upon separately to satisfy Required Minimum Distribution rules for each separate account.
2	For IRAs and 403(b) accounts, any one or more accounts can be drawn upon to satisfy the requirements for all accounts. The requirement is calculated in the aggregate; however, IRAs can only be aggregated with IRAs, and 403(b)s can only be aggregated with 403(b)s.
3	IRA and 403(b) plans held as an owner/employee may not be aggregated with IRAs held as a beneficiary.
4	Withdrawals from a Roth IRA cannot be aggregate, nor will they satisfy any portion of the Required Minimum Distribution.
5	If any portion of the IRA or 403(b) account has been annuitized, the annuitized and non-annuitized portions are treated as separate plans. Distributions received from the annuitized portion cannot be aggregated with the non-annuitized portion for purposes of satisfying the Required Minimum Distribution. The non-annuitized portion must calculate the Required Minimum Distribution separately excluding the annuity contract from the account value.

4. Required Beginning Date ("RBD"). The date on which lifetime distributions to a Plan Participant from the IRA/Plan must begin. This date is April 1st of the calendar year following the later of: (a) the calendar year in which the Plan Participant reaches the age of 72 (or age 70 ½ applies for those who reached age 70 ½ before January 1, 2020); or (b) the calendar year in which a Plan Participant retires from

being employed by the company which maintains the Qualified Retirement Plan, provided that the exception in clause (b) does not apply if the Plan Participant is at least a 5% owner of the employer company who sponsors the Plan. Because the CARES Act eliminated Required Minimum Distributions for the calendar year 2020, Plan Participants who otherwise would reach their Required Beginning Date in 2020 do not need to commence taking Required Minimum Distributions until 2021.

ILLUSTRATION 2.4 – MINIMUM DISTRIBUTION RULES FOR ORIGINAL PARTICIPANT AND/OR ROLLOVER SURVIVING SPOUSE

Type	Rule
Roth IRA	No distribution required during lifetime.
Non 5% owner of company sponsoring IRA/Plan	No distributions required until the later of the Required Beginning Date ("RBD") or retirement
5% or more owner of company sponsoring IRA/ Plan	No distributions until after RBD, regardless of retirement status.
All other Qualified Retirement Plans and IRAs	No distributions until after RBD, regardless of retirement status.

ILLUSTRATION 2.5 – ANOTHER WAY OF LOOKING THE SIX METHODS

Notable Differences in Distribution Rules when Plan Participant Dies Before or After his or her Required Beginning Date (RBD)		
	If Plan Participant Dies Before Required Beginning Date	**If Plan Participant Dies After Required Beginning Date**
Surviving Spouse Beneficiary	If sole beneficiary, distributions do not have to begin until the later of: (a) the year after the Plan Participant dies, or (b) the year when the Plan Participant would have reached the RBD. If both (a) the Plan Participant, and (b) the Surviving Spouse, as beneficiary of a Conduit Trust, die before Plan Participant's	Unless Surviving Spouse rolls the IRA/Plan over into his or her own IRA, distributions will begin in the year after the Plan Participant dies based upon the Surviving Spouse's life. If the Surviving Spouse's life expectancy is shorter than the deceased Plan Participant, then the life expectancy of the Plan Participant may continue to be used under the At-Least-As-Rapidly Rule.

Notable Differences in Distribution Rules when Plan Participant Dies Before or After his or her Required Beginning Date (RBD)		
	If Plan Participant Dies Before Required Beginning Date	**If Plan Participant Dies After Required Beginning Date**
	RBD, and the Trust does not otherwise qualify as a See-Through Trust, the IRS previously ruled that there is no Designated Beneficiary, so that the 5-Year Rule must apply.	
Individual Non-Spouse Beneficiary	The Designated Beneficiary's life expectancy is used based on the Non-Recalculated One Life Method if Plan Participant died prior to January 1, 2020. If Plan Participant died on or after January 1, 2020, then the 10-Year Rule applies unless the beneficiary is an Eligible Designated Beneficiary, and no distributions are required until the end of the 10th year following the death of the Plan Participant.	If Plan Participant died prior to January 1, 2020: (a) Use Designated Beneficiary's life expectancy OR (b) If the non-spouse beneficiary is older than the Plan Participant, then the life expectancy of the Plan Participant may continue to be used under the "At-Least-As-Rapidly Rule". The Non-Recalculated One Life Method is still used if the Plan Participant died before January 1, 2020. If Plan Participant died on or after January 1, 2020, then the 10-Year Rule applies unless the beneficiary is an Eligible Designated Beneficiary; however because the Plan Participant died after his or her Required Beginning Date distributions must be made in years 1-9 based on the life expectancy of the Designated Beneficiary using the Non-Recalculated One Life Method until the 10th year when all assets are distributed.
No Designated Beneficiary	The 5-Year Rule applies - all funds must be distributed on or before December 31st of the 5th year following the date of the death of the Plan Participant; provided that, for Plan Participants who have died between January 1, 2015 and December 31, 2019, the 5-Year Rule has become a "6-Year Rule," whereby all funds must be	"At-Least-As-Rapidly Rule" applies - distributions continue to be paid out over the remaining life expectancy of the deceased Plan Participant, based upon the Non-Recalculated One Life Method is still used.

Notable Differences in Distribution Rules when Plan Participant Dies Before or After his or her Required Beginning Date (RBD)		
	If Plan Participant Dies Before Required Beginning Date	**If Plan Participant Dies After Required Beginning Date**
	distributed before December 31st of the sixth year following the death of a Plan Participant, which is because of the CARES Act having eliminated the requirement that Required Minimum Distributions be made in the calendar year 2020.	

For more discussion of the differences in rules if the Plan Participant died on or after January 1, 2020, see Chapter 7.

5. Required Beginning Date First Year Delay Right. A Plan Participant who has reached the age of 72 (or age 70½ for a Plan Participant who has reached age 70½ before January 1, 2020), or who has retired from being employed by the company which maintains the Qualified Retirement Plan (under certain circumstances), can take some or all of the first year Required Minimum Distributions on any day or days during the calendar year in which either of the above events has occurred, or by April 1st of the following calendar year (his or her Required Beginning Date). Therefore, the first two annual Required Minimum Distributions could be taken during the calendar after the year in which the Plan Participant has reached the age of 72 (or 70½, if before January 1, 2020), or has retired from working for the company which sponsors the Qualified Retirement Plan (by April 1st as to payments required for the first year, and by December 31st as to the payments required for the second year). The CARES Act has eliminated the requirement that Required Minimum Distributions be made in the calendar year 2020, so a Plan Participant who has reached his or her Required Beginning Date in 2020 is not required to take his or her 2020 Required Minimum Distributions until 2021. Additionally, if the Plan Participant did not take his 2019 Required Minimum Distributions before April 1, 2020, then such 2019 Required Minimum Distribution also can be postponed until April 1, 2021.

   The Plan Participant should consult with a tax advisor before or after reaching the Required Beginning Date to determine whether the "first year required payment" should be deferred until the following year, based upon the expected tax bracket or rates of asset growth applicable to the Plan Participant.

   If the Plan Participant is going to be in the highest tax bracket in both years, then it makes sense to defer the entire first year Required Minimum Distribution until the second year. If the Plan Participant is not in the highest tax bracket, then it makes sense to "run the numbers" to determine how to best reduce or defer the tax liability, after taking into account the value of deferring the payment of federal income tax. Nevertheless, the Plan Participant is considered to have reached his or her Required Beginning Date on April 21, 2020 notwithstanding that no Required Minimum Distribution must be made in 2020.

Example (see Illustration 2.6 below)[43] -

Claire reaches age 72 on May 1, 2022 and has a Required Minimum Distribution of 3.65% of the account balance that must be taken prior to April 1, 2023, and a 3.77% distribution that must be taken prior to December 31, 2023. Claire can pay the above percentages in 2022 and 2023 or may elect to make a 3.65% payment of the 2022 account balance and a 3.77% payment of the 2021 account balance, both in 2023. The amount that would have been paid out in 2022 does not reduce the balance of the amount held in the plan that is used to determine the 2023 Required Minimum Distribution amount. For example, if the account is worth $1,000,000 as of December 31, 2020 and grows by 5.00% during the subsequent two years, then Claire could have distributed 3.65% ($38,325.00) in 2020 and 3.77% ($40,047.15) in 2021 for a total of $78,372.15. If Claire waits until 2021 to satisfy *b*oth years, then the total amount paid will be $79,889.25.

[43] The numbers will be updated when the next edition of the book is released, which will be shortly after the Proposed Regulations are finalized.

ILLUSTRATION 2.6 -- DEADLINES FOR REQUIRED MINIMUM DISTRIBUTIONS

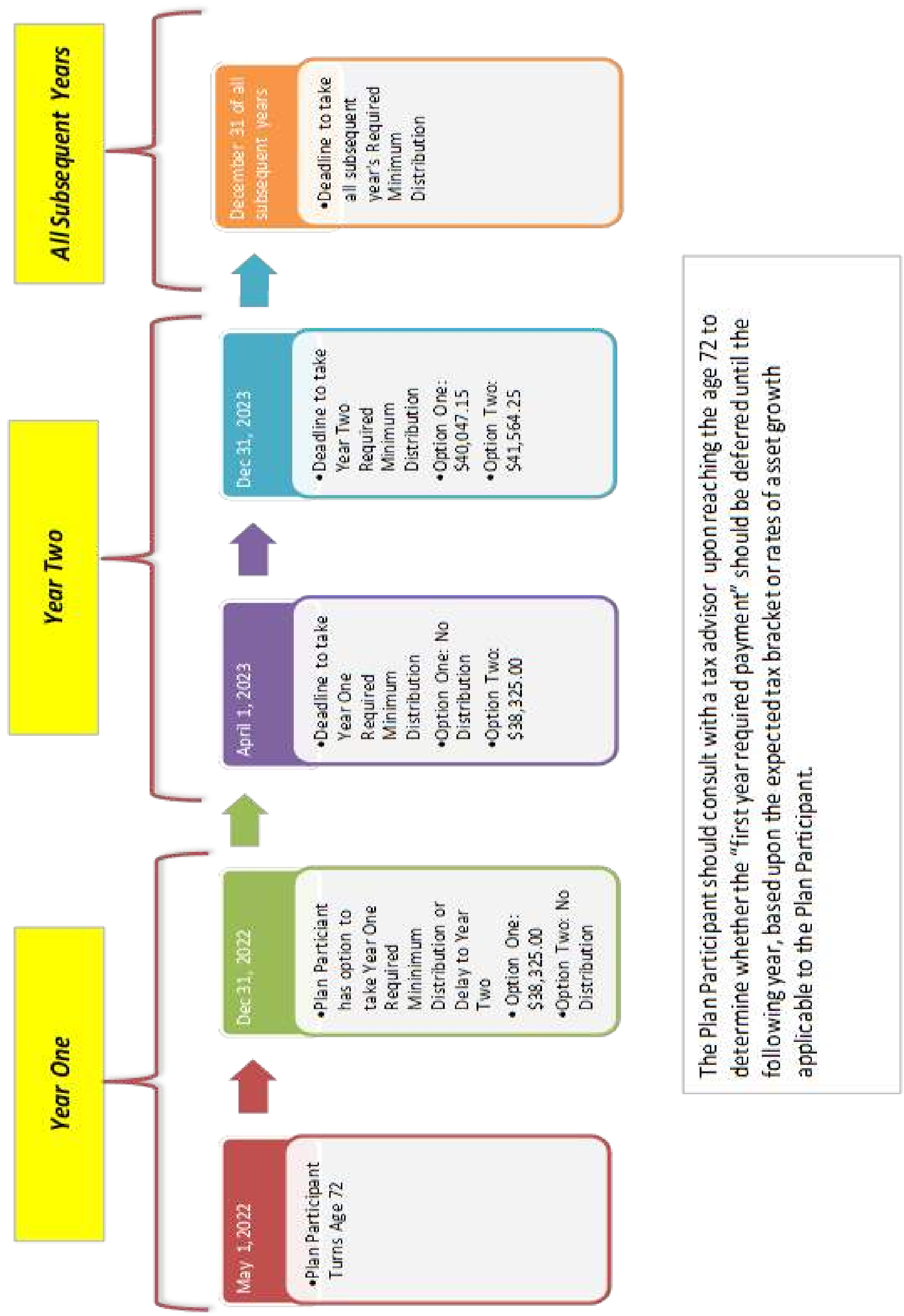

ILLUSTRATION 2.7 - OPTION ONE - NO DELAY OF FIRST YEAR DISTRIBUTION

Year	Beginning Balance	Growth 5%	Year End Balance	Required Distribution	Amount Deferred	Ending Balance After Distribution	Difference
5/1/2022	$-					$1,000,000	$-
5/1/2022-12/31/2022	$1,000,000	$50,000.00	$1,050,000.00	($38,325.00)	$-	$1,011,675.00	($38,325.00)
1/1/2023-12/31/2023	$1,011,675.00	$50,583.75	$1,062,258.75	($40,047.15)	$-	$1,022,211.60	($399.15)

OPTION TWO - DELAY FIRST YEAR DISTRIBUTION

Year	Beginning Balance	Growth 5%	Year End Balance	Required Distribution	Amount Deferred	Ending Balance After Distribution	Difference
5/1/2022	$1,000,000.00					$1,000,000.00	
5/1/2022-12/31/2022	$1,000,000.00	$50,000.00	$1,050.000.00	($38,325.00)	$38,325.00	$1,050,000.00	$38,325.00
1/1/2023-12/31/2023	$1,050,000.00	$52,500.00	$1,102,500.00	($79,889.25)	$-	$1,022,610.75	$399.15

6. Required Beginning Date First Year Delay Crossover Analysis. What after tax rate of return on investments would a hypothetical 37% tax bracket IRA owner need to earn to make it worthwhile to delay taking the first year minimum distribution, after accounting for the excess amount that has to be paid out (but later) if the first year payment is moved from December 31st of the year before reaching the Required Beginning Date to April 1st of the year in which the Plan Participant reaches the Required Beginning Date?

   Based upon the following (Illustrations 2.7 & 2.8), we believe that the rate of return is approximately 2.39%. A return below this level would not generate enough tax-deferred growth to offset the additional tax owed in the second year. However, in light of the CARES Act eliminating the requirement for Required Minimum Distributions being made in 2020, it may be worthwhile to consider the additional year of deferral that could apply where the Plan Participant would have reached his or her Required Beginning Date in 2020 and has not yet taken his or her first Required Minimum Distribution.

ILLUSTRATION 2.8 --
REQUIRED BEGINNING DATE FIRST YEAR DELAY CROSSOVER ANALYSIS

IRA Rate of Return	Option One - No Delay of RMD	Option Two - Delay First Year's RMD	Difference (Two - One)
1.00%	$96,677.33	$96,639.87	$(37.46)
2.00%	$98,601.21	$98,590.34	$(10.87)
3.00%	$100,544.04	$100,564.16	$20.12
4.00%	$102,505.83	$102,561.43	$55.60
5.00%	$104,486.57	$104,582.28	$95.71
6.00%	$106,486.27	$106,626.81	$140.54
7.00%	$108,504.92	$108,695.13	$190.21
8.00%	$110,542.53	$110,787.37	$244.84

ILLUSTRATION 2.9 –
AGE 70½ FIRST YEAR DELAY CROSSOVER ANALYSIS

7. <u>Other Considerations with Respect to Whether to Delay the First Year Minimum Distribution</u>.

(a) Social Security Benefits – Social Security benefits become taxable if "provisional income" exceeds a certain amount. Provisional income is generally based upon the Plan Participant's gross income, plus tax exempt interest, excluded foreign income, and one-half of Social Security benefits.

Distributions from retirement plans count for the purpose of determining if tax is owed on Social Security benefits and are considered part of the provisional income.[44] Therefore the effect on the taxability of Social Security payments should be considered in deciding when to take the first year's Required Minimum Distribution.

A chart and explanation of the taxation of social security benefits is as follows:

TAXATION OF SOCIAL SECURITY BENEFITS

	Provisional Income	**Percentage of Social Security Taxable**
Single or Married Filing Separately	Below $25,000	All SS income is tax-free
	Between $25,000-$34,000	Pay income tax on up to 50% of benefits
	$34,000 and up	Up to 85% of income is taxable
Married Filing Jointly	Below $32,000	All SS income is tax-free
	Between $32,000-$44,000	Pay income tax on up to 50% of benefits
	$44,000 and up	Pay income tax on up to 85% of benefits

Plan Participants may want to stay below the incremental levels at which their Social Security benefits become subject to the 50% or 85% of otherwise taxable rate that applies.

(b) Audit Risk – The IRS launched a major initiative in 2014 to crack down on Plan Participants who do not distribute their Required Minimum Distributions. If a Plan Participant decides to delay the first year's Required Minimum Distribution, he or she will check the box that indicates to the IRS that the Plan Participant is past the Required Beginning Date and distributions are required, however, the Plan Participant will report no distribution and have no 1099-R on file. This could raise a red flag even though the Plan Participant has not done anything wrong.

(c) Possible Deductible Health Related Expenses – Many taxpayers who reach age 72 may have significant health or nursing needs or a spouse with significant health or nursing needs. Such expenses may be deductible to the extent exceeding 10% of adjusted gross income in 2020. It will make sense to withdraw as much from an IRA/Plan as would be needed to take full advantage of any such significant deductions when the Plan Participant or his or her spouse can avoid paying any income tax on distributions when there are significant deductible medical expenses.

[44] I.R.C. § 86.

(d) Avoiding the Confusion - As discussed above, the two Required Minimum Distributions will be computed using different account balances, different divisors, and have different deadlines. The simplest option is to just take the entire first year's Required Minimum Distributions on or before December 31st in the year the Plan Participant reaches the Required Beginning Date.

8. Other Income Tax Planning Considerations, Opportunities, and Traps.

OPPORTUNITIES:

(a) Estimated Taxes Coordination Opportunity – A Plan Participant can withhold federal income tax from Required Minimum Distributions by filing a Form W-4P. The tax withheld from retirement plan distributions is treated as if it was paid equally on each of the due dates for estimated tax payments. § 6654(g)(1). Therefore, a distribution from a retirement plan paid on December 31st but withheld for income tax purposes will be treated as if it had been divided into four equal payments made on March 31st, June 30th, September 30th, and December 31st. For example, a $100,000 distribution on December 31st will be treated as if $25,000 was paid on March 31st, $25,000 on June 30th, $25,000 on September 30th, and $25,000 on December 31st. This effectively allows a Plan Participant to delay paying estimated taxes until the end of the calendar year.

Be wary as this strategy becomes more risky the older the Plan Participant gets. If the Plan Participant dies before the Required Minimum Distribution is used to pay taxes, then the estate can become liable for the penalty on underpayment of income taxes in the year of the Plan Participant's death.[45]

(b) Appreciated Employer Stock Withdrawal Opportunity – A Plan Participant in an employee sponsored retirement plan has the opportunity to withdraw a lump sum distribution from the account and only be taxed on a portion of the withdrawal. The taxable portion is the excess of the value of the stock over the plan's transferred basis (what the stock was originally purchased for). The remaining portion is treated as "net unrealized appreciation" (NUA) and is not taxable until the stock received is sold by the recipient. This net unrealized appreciation, and also subsequent appreciation, is taxed at long-term capital gains rates when sold. This can result in significant tax savings for the Plan Participants whose ordinary income rates are much higher than the capital gains rate.[46]

For example, a CEO in the 37% tax bracket holds $100,000 in company stock upon retirement. The stock was originally purchased for $20,000. The CEO has the option to either distribute all of the company's stock or roll the

[45] See Natalie Choate's seminar outline entitled *The 201 Best and Worst Planning Ideas for Your Client's Retirement Benefits* (available at www.ataxplan.com) at 3-11.
[46] *Id*. at 3-12.

stock into an IRA account subject to the Required Minimum Distribution rules.

If he chooses to distribute all of the stock and elects to use the net unrealized appreciation tax treatment, then the tax on the distribution would be $7,400 (37% x cost basis of $20,000). He then immediately sells the stock triggering a capital gains tax of $19,040 (23.8% x net unrealized appreciation of $80,000). The CEO would pay total tax of $26,440.

If the CEO instead rolled the employer plan into an IRA, the results would be much different. The CEO would pay ordinary income tax on the entire balance, resulting in total tax of $37,000. By using net unrealized appreciation tax treatment, the CEO would be able to save $10,560 in taxes.

Whether the net unrealized appreciation tax treatment will be beneficial depends on a number of factors, some of which include the following:

(i) Tax rates;

(ii) The amount of Net Unrealized Appreciation;

(iii) The length of time until the distribution; and

(iv) Age of participant (individuals born before 1936 are eligible for a special averaging tax rate).[47]

As a general rule, the shorter the Plan Participant plans to keep the assets in the plan, the more attractive Net Unrealized Appreciation tax treatment becomes. However, if the Plan Participant plans to keep the assets under an IRA for a longer period of time, the benefits of tax deferral become more attractive.

(c) <u>There is no requirement that Required Minimum Distributions be paid in cash</u>.

A Plan Participant has the option of taking distributions in kind to avoid having to have the IRA sell assets and distribute cash. The Plan Participant receiving a distribution of stock or other IRA assets must include them in ordinary income based upon the fair market value on the date of the distribution, which becomes the Plan Participant's tax basis upon subsequent sale. This could be beneficial for two reasons:

[47] *Id.* at 3-13.

(i) Taking Required Minimum Distributions in kind saves commissions on selling the investment and then re-buying the investment outside the plan.

(ii) Once distributed, any post distribution gain will be taxed at capital gains rates rather than at ordinary income when distributed from the IRA. Therefore, assets that are currently undervalued or assets that are considered to be growth stocks are the best candidates for in kind distributions.

Natalie Choate points out that there is limited guidance available on how to determine what the "fair market value" of securities on the date of distribution, and therefore recommends that "unless there is a good reason to do otherwise, pay RMDs in cash."[48]

(d) Convert to Roth in low income tax years or marry someone with significant ordinary losses and convert to a Roth! – If a Plan Participant experiences a significant drop in income or significant deductible expenses in a given year, then he or she should consider converting all or a portion of a Plan into a Roth IRA. The Plan Participant will have to pay tax on the amount converted at ordinary income rates but will pay no tax on later distributions. By converting into a Roth IRA in low income tax years, the Plan Participant can take advantage of the lower tax rate now and not be subject to a higher tax rate in subsequent years. Roth IRA conversions do not trigger the 10% excise tax that will otherwise apply to individuals under age 59½, and the income limitations that exist for Roth IRA contributions do not apply to IRA conversions. A Plan Participant can convert a retirement plan into a Roth regardless of income level.

(e) Basis-ectomy – separating the coffee from the cream.[49]

A Plan Participant can roll the taxable portion from a non-IRA Qualified Retirement Plan into a traditional IRA or another Qualified Retirement Plan, and the remaining balance of the original Qualified Retirement Plan equal to the amount contributed by the Plan Participant can be distributed tax free.[50]

This opportunity is only available if the Qualified Plan accepts rollovers from traditional IRA's.

TRAPS

(a) IRA to HSA Account transfers may not be beneficial. The income tax deduction for contributions to an HSA is worth more than being able to take

[48] *Id.* at 3-16.
[49] *Id.* at 3-31.
[50] IRS Notice 2014-54.

a Required Minimum Distribution tax free by funding an HSA from an IRA in most situations. It may, however, be best to fund the HSA from an IRA under the following circumstances:[51]

(i) An individual under the age of 59½ with no other liquid investments funds his or her HSA to avoid the 10% penalty on early distributions.

(ii) An individual wants to avoid having an IRA distribution appear on his or her bank account due to creditor concerns, financial aid considerations, and ex-spouse or state income tax effects.

(b) <u>The Required Minimum Distribution Rules continue to apply through the year of the Plan Participant's death as if the Plan Participant was still living</u>. This means that beneficiaries will be responsible for ensuring that any Required Minimum Distribution that has to be made before the end of the calendar year in which the Plan Participant died is timely distributed. There will be many situations where the Plan Participant has been very sick and has not taken his or her Required Minimum Distribution, and then the surviving family members and fiduciaries are not able to ascertain what the situation is until it is too late. When this occurs, it is best to take the distribution as soon as possible in the following calendar year, and to request that the IRS abate penalties. The penalty for an untimely Required Minimum Distribution is 50% of the amount that should have been distributed but was not distributed timely.

(c) <u>Withdraw Early?</u> Some advisors counsel Plan Participants to withdraw money from an IRA or retirement plan (or to complete a Roth IRA conversion) early when both estate tax and income tax are expected to apply. The only effect that an early withdrawal has is the loss of the income tax deferral that a retirement plan provides, or the ten percent (10%) penalty tax that is imposed if the withdrawal is not rolled over into another IRA, and the Plan Participant is under the age of 59½.[52]

<u>Note</u> – If a retirement plan will be cashed out shortly after the death of an estate taxable Plan Participant, it will often be best to cash out the IRA/Plan before the death of the Plan Participant. If the IRA/Plan was cashed out after death, the beneficiary would receive an income tax deduction (but not a credit) under Internal Revenue Code Section 691(c) for any federal estate taxes paid on the IRA/Plan; however, this deduction may be limited due to the phase out of itemized deductions at a certain level of income. Also, the beneficiary will not receive a deduction for state estate taxes paid on the IRA/Plan. Therefore, in certain situations, it may make sense to cash out the IRA/Plan before the death of the Plan Participant.[53]

[51] Choate's *The 201 Best and Worst* at 3-18 and 3-19.
[52] Choate's *The 201 Best and Worst* at 3-72.
[53] Choate's *The 201 Best and Worst* at 3-72.

It can certainly make sense to withdraw monies from an IRA/Plan as needed to enable an estate taxable client to make gifts and to engage in other appropriate planning techniques where the IRA constitutes the only liquid asset available and borrowing or selling other assets is for some reason not feasible for tax, financial, or emotional reasons.

(d) Wash Sales Rules Extend to Securities Purchased by IRA Accounts – Clients who would like to sell an individually owned stock or mutual fund to trigger capital losses may wish to immediately purchase the same security under an IRA. The wash sale rule states that a Plan Participant cannot deduct a loss on the sale of securities if a substantially identical security is repurchased within thirty days after the loss- generating sale.[54] According to Revenue Ruling 2008-5, the sale of a security outside of an IRA will be matched with the purchase of a security inside an IRA/Plan for the purposes of applying Internal Revenue Code Section 1091. Therefore, the repurchase under an IRA/Plan needs to take place more than thirty days after the original sale to avoid the wash sale rule.[55]

9. Distribute or Sell Hard-to-Value Assets As Soon As Possible. Currently, IRA providers have the option to check the box and "flag" hard-to-value assets on Forms 5498 and the 1099-R. Some commentators believe that this reporting requirement is likely to become mandatory soon.[56] The Plan Participant should either sell the asset in an arm's length transaction to an unrelated party or distribute the asset as part or all of a Required Minimum Distribution. It would make sense to get this done sooner rather than later in order to avoid attracting an audit.

10. Rules and Other Considerations for Roth IRA Conversions.

(a) A Plan Participant who expects his or her income tax bracket to be higher in the future may be well advised to convert an IRA into a Roth IRA.

(b) An individual who retired after age 59½, but has not yet reached his or her Required Beginning Date (April 1st of the year in which he or she reaches age 72, or age 70½ prior to January 1, 2020) should consider a Roth IRA Rollover if he or she has significantly less income, or significant deductible expenses, and is therefore in a lower than normal tax bracket. The tax bracket will most likely increase when distributions are forced out of the Plan at the Required Beginning Date; therefore, a Roth IRA rollover can be used to take advantage of the then lower income tax bracket.[57]

(c) One reason not to convert into a Roth IRA is that the money paid in taxes may be needed later. More often than not, clients spend down relatively large IRAs during their last years "tax free" due to the medical expense

[54] I.R.C. § 1091.
[55] Choate's *The 201 Best and Worst* at 3-37.
[56] Choate's *The 201 Best and Worst* at 3-16 and 3-17.
[57] Choate's *The 201 Best and Worst* at 3-56 and 3-57.

deduction. These clients may have run out of money had the IRA been converted into a Roth IRA.[58]

11. Rolling over from Qualified Retirement Plan into an IRA will give a Plan Participant more options.

Some Qualified Retirement Plans only allow the death benefit (the balance of plan assets on death) to be payable in a lump sum. Therefore, Plan language should be checked to see if distribution election options preferred for a particular Plan Participant are permitted. Even if the stretch options are available, an employer could terminate a plan resulting in a lump sum distribution. A Qualified Retirement Plan Participant should consider rolling plan benefits over to an IRA as soon as this can occur, if the Participant is leaving the benefits to (a) a non-spouse Designated Beneficiary who would want to stretch the payout over his or her life expectancy, or (b) an Accumulation Trust or Conduit Trust where an individual will be the Designated Beneficiary for plan distribution determination purposes in order to avoid these potential pitfalls.[59]

403(b) plans can only be invested in annuity contracts or mutual funds offered by the plan, whereas IRAs offer much more flexibility than a 403(b) plan or the typical Qualified Retirement Plan. Qualified Retirement Plans may also assess administrative expenses and costs against Participant's accounts.

Normally any Plan Participant who is not an individual who has reached age 59½ will have to pay a 10% penalty in income withdrawn from the qualified IRA/Plan, however some of the exceptions to the penalty are available only to IRAs.[60]

12. Reasons to Leave Benefits in Qualified Retirement Plan.

(a) With Qualified Retirement Plans, the Participant may be able to borrow funds, have the plan own life insurance, or collectibles.

(b) A non-spouse beneficiary may be able to roll over an inherited Qualified Retirement Plan into his or her own inherited Roth IRA. This option will not be available if the Plan Participant rolls over the Qualified Retirement Plan into an IRA before his or her death.[61]

(c) An individual who has reached age 55 will not be subject to the 10% penalty on withdrawals from a Qualified Retirement Plan if the individual has separated from service on or after reaching age 55.

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[58] See LISI Employee Benefits & Retirement Planning Newsletter #549 (November 9, 2010) at http://www.leimbergservices.com, by Alan S. Gassman, Kenneth J. Crotty, and Christopher J. Denicolo, entitled One Good Reason Not To Do A Roth IRA Conversion.

[59] Choate's *The 201 Best and Worst* at 3-26.

[60] *Id.*

[61] *Id.*

(d) Under an IRA (but not a Qualified Retirement Plan), a Participant can elect to receive substantially equal periodic payments for life and avoid the 10% excise tax on those amounts received.

If Qualified Retirement Plan monies have been mixed with IRA contribution monies, the bankruptcy exemption rules will be challenging at best.[62]

13. Rollovers from Qualified Retirement Plans should be kept separate from regular IRA plans. Rollovers from Qualified Retirement Plans should be kept separate from regular IRA plans. The federal bankruptcy court exemption rules limit protection for IRAs held by residents of states that do not have IRA creditor protection to $1,362,800 as of 2020 (indexed for inflation and adjusted every three years; the next adjustment will occur in 2022) for IRAs that have been funded with annual contributions.

14. Asset Allocation Rules. While many financial planners will balance IRA and non-IRA investments using the same ratios of fixed income to equity, a good many financial advisors believe that the better approach is to have taxable bonds and equivalent fixed income investments under IRAs, with equities outside of the IRAs. Equities are tax advantaged because the capital gains on sale will not occur until sold, and qualified dividend income is taxed between 0% and 23.8% (including the 3.8% Medicare tax when applicable). Taxable interest earned on bonds and assets that would cause short term capital gains, such as hedge fund holdings, may be held under an IRA, which would otherwise turn long term capital gains into ordinary income if equities are held under the IRA.[63]

15. Annuitized IRA. An IRA can be "annuitized" by investing the IRA assets in an annuity contract whereby the insurance carrier issuing the contract will make a series of annual or more frequent equal lifetime payments to the IRA owner. These payments will be considered to satisfy the Required Minimum Distribution rules for the value of the annuitized annuity but will not be considered to satisfy or apply towards the Required Minimum Distribution for the remaining non-annuitized IRA value. The annuitized payments will typically exceed the Required Minimum Distribution amounts that would otherwise have applied.

For example, a male age 70 who is otherwise subject to the payout amounts described in Illustration 2.1 above might instead cause his IRA to purchase an annuitized contract that would require payment of 7.67% of the initial amount

[62] The rule reads as follows, and no one knows how it will work: "For assets in individual retirement accounts described in section 408 or 408A of the Internal Revenue Code of 1986, other than a simplified employee pension under section 408(k) of such Code or a simple retirement account under section 408(p) of such Code, the aggregate value of such assets exempted under this section, without regard to amounts attributable to rollover contributions under Sections 402(c), 402(e)(6), 403(a)(4), 403(a)(5), and 403(b)(8) of the Internal Revenue Code of 1986 and earnings thereon, shall not exceed $1,000,000 in a case filed by a debtor who is an individual, except that such amount may be increased if the interests of justice so require." 11 U.S.C. § 522.

[63] Choate's *The 201 Best and Worst* at 3-37.

invested each year for his lifetime. Alternatively, a female might cause her IRA to purchase an annuitized contract that would require payment of 7.12% of the initial amount invested each year for her lifetime.

Payments received from an annuitized IRA by a Plan Participant who has not reached age 59½ will not be subject to the 10% excise tax described below.

Below (Illustration 2.10) is an example provided by one investment company of hypothetical payments for a male and female age 70 who annuitizes $100,000 of his or her IRA to receive lifetime payments that will never run out in lieu of minimum distributions which would be less.

ILLUSTRATION 2.10 –
ANNUITIZED IRA PAYOUTS ON $100,000 INVESTMENT BY AN INDIVIDUAL AGE 70

	Monthly	Yearly	% of Premium Each Year for Life
Male	$639.00	$7,668.00	7.67%
Female	$593.00	$7,116.00	7.12%

16. <u>Qualified Longevity Annuity Contract (“QLAC”)</u>. A QLAC is an annuity contract held under an IRA that begins paying a lifetime annual (or more frequent) annuity amount one or more years after acquisition. Before going into payment mode, the value of a QLAC is not counted in determining Required Minimum Distribution payment amounts. When payments begin, they must be distributed in full each year and will normally exceed the Required Minimum Distribution amount until the client reaches a fairly high age (upper 80s and older). The Treasury Regulations released on July 2, 2014 permit the lesser of $145,000 for 2022 (the amount is adjusted for inflation and was previously set at $135,000 for 2021 and 2020) or 25% of a taxpayer’s applicable IRA balances to be held under QLAC contracts that need not be included in the value of the IRA for the purposes of determining Required Minimum Distribution.[64] Versions of the SECURE Act 2.0 in both the House and Senate, as of June 2022, would remove the 25% cap, and the Senate bill would increase the cap $200,000.[65] The contract will pay fixed dollar amounts at stated intervals over a number of years for the life of a Plan Participant, beginning no later than age 85. If the Plan Participant dies before he or she has received payments equal to the amount paid for the contract, then the contract may offer a return of premium option so that the Plan Participant in effect receives back all amounts invested without interest. However, this return of premium option is not required by the Regulations and will cause reduction in the minimum annual amounts paid. The lesser of $145,000/25% limitation can be somewhat confusing and is described with further detail in LISI Employee Benefits and Retirement

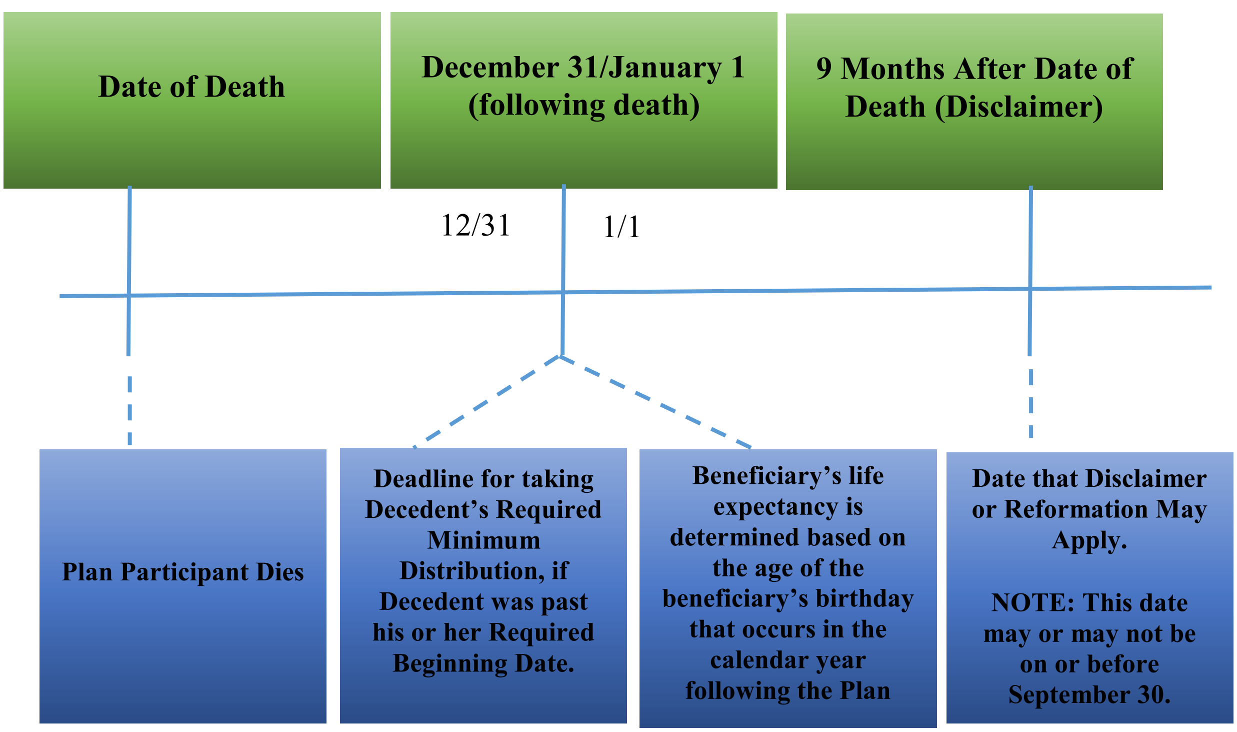
[64] Reg. § 1.401(a)(9)-6, Q&A-17(b)(2), -17(d). Notice 2021-61, Notice 2020-79, Notice 2019-59.

[65] Sarah O’Brien, *Some ‘SECURE 2.0’ Retirement Proposals In The Senate Look Different From The House Version. Here Are Key Provisions Under Consideration*, CNBC, (June 26, 2022, 8:00 AM), https://www.cnbc.com/2022/06/26/not-all-secure-2point0-proposals-in-the-house-and-senate-are-the-same.html.

Planning Newsletter #639 (August 20, 2014) at http://www.leimbergservices.com, by Alan Gassman, Christopher Denicolo & Brandon Ketron: A Practical Approach to Qualifying Longevity Annuity Contracts (QLACs) - Using the (King) L.E.A.R. (Life Expectancy And Return) Analysis to Determine Whether Clients Should Invest in Specially Designed Annuity Products under Their IRA or Qualified Retirement Plans, located in Appendix D.17.Require the Plan Administrator to Provide Information to Beneficiaries and Their Fiduciaries. This can be accomplished by adding the following language to the beneficiary designation:

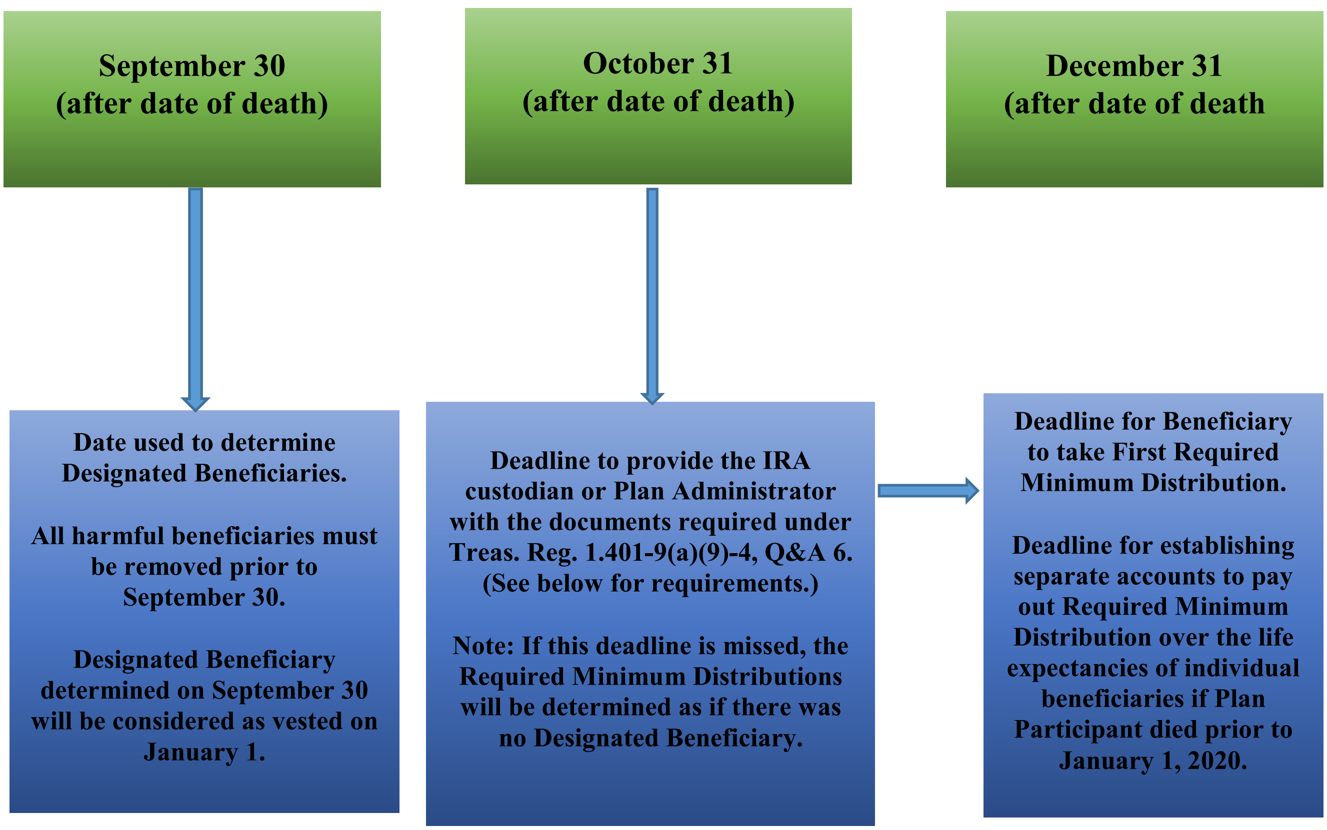
"Being plan administrator shall provide any personal representative of my estate, any trustee of the John Smith Living Trust, and any lawyer confirming that he or she represents one or more of the above fiduciaries with any and all information reasonably requested, including a copy of this beneficiary designation, a copy of the applicable IRA/Plan, and all information needed to facilitate performance of duties and planning concerning such account, including specifics on the assets therein they hold and distribution options."

ILLUSTRATION 2.11 –
DEADLINES AFTER DEATH OF PLAN PARTICIPANT



Documents required to be provided to Plan Administrator according to Treas. Reg 1.401(a)(9)- 4, Q&A 6 - In order to satisfy the documentation requirement for Required Minimum Distributions after the death of the Plan Participant, by October 31st of the calendar year immediately following the calendar year of the employee's death, the trustee of the trust must either (1) provide the plan administrator with a final list of all beneficiaries of the trust (including contingent and remaindermen beneficiaries with a description of the conditions on their entitlement).

ILLUSTRATION 2.12 – DEADLINES AFTER DEATH OF PLAN PARTICIPANT



as of September 30 of the year following the year of the Plan Participant's death and certify that, to the best of the trustee's knowledge, this list is correct and complete and that the requirements of Treas. Reg. § 1.401(a)(9)- 4, Q & A-5(b)(1), (2), and (3) are satisfied and agree to provide a copy of the trust instrument to the plan administrator upon demand or (2) provide the plan administrator with a copy of the actual trust document for the trust that is named as a beneficiary of the employee under the plan as of the Plan Participant's date of death.

18. Planning for Mentally Disabled Plan Participant. - It may be possible to use a restricted IRA agreement or an Individual Retirement Trust to limit a Plan Participant's access to the IRA/Plan funds in order to protect against the possibility of mental deterioration leading to poor financial decision-making.

PLR 201150037 blessed a custodial IRA arrangement in which the participant and custodian agreed to a series of "directions," which generally imposed a thirty-day delay on any request for distributions to the account. The goal of the "directions" was to protect an individual who suffered from bipolar disorder and would go on uncontrolled spending binges. The thirty-day delay period enabled the individual to countermand the request for distributions at any time during the thirty-day period following a request. It is unclear if this ruling would be extended to cover longer time periods or more restrictive "directions."[66]

19. See-Through Trust – An Accumulation Trust or a Conduit Trust, as used by the IRS, to denote a trust that may not be considered as a Non-Person if the trust is named beneficiary of an IRA/ Plan. Assuming that certain requirements are met, and that the trust qualifies as a Conduit Trust or as an Accumulation Trust, the trust is "looked through" to the Designated Beneficiary for the purpose of determining the Applicable Payment Mode of Required Minimum Distributions.

20. Accumulation Trust – And Discussion of How These Have Changed After The SECURE Act. A trust that is the beneficiary of an IRA/Plan where the trustee has the power to accumulate some or all of the Required Minimum Distributions and other payments from the IRA/Plan (i.e., the terms of the trust instrument do not require the trustee to distribute all Required Minimum Distributions and all other payments from the IRA/Plan to a particular beneficiary) that also qualifies as a "See-Through Trust." Thus, the Trustee can accumulate monies or other investments for later use. Such trust can have no Non-Person Tier I or Tier II Beneficiaries after September 30th of the calendar year following the death of the Plan Participant (i.e., the Designation Date) and must properly register certain information with the Plan Administrator by October 31st of such calendar year in order to qualify as an Accumulation Trust. Under the SECURE Act, where a Plan Participant has died on or after January 1, 2020, the Accumulation Trust will most likely be subject to the 10-Year Rule, unless it is for the sole lifetime benefit of a chronically ill or disabled beneficiary, or the Accumulation Trust qualifies for the Minor Child Accumulation Trust Exception or an Age 31 Outright Distribution Accumulation Trust. Nevertheless, disabled and chronically ill beneficiaries are the only Designated Beneficiaries that can qualify an Accumulation Trust for a Life Expectancy payout without the 10-Year Rule applying at some point, and the determination of whether a beneficiary is disabled or chronically ill is made upon the date of the Plan Participant's death. Even a Surviving Spouse who is the Designated Beneficiary of an Accumulation Trust cannot qualify the trust for a lifetime payout, if the Plan Participant died after 2019, unless he or she is chronically ill or disabled on the date of the Plan Participant's death.

If the Plan Participant died on or after January 1, 2020 (the effective date of the SECURE Act), then an Accumulation Trust will be subject to the 10-Year Rule

[66] For further discussion on PLR 201150037, see LISI Employee Benefits & Retirement Planning Newsletter #597 (February 15, 2012) at http://www.leimbergservices.com, "Disability Planning for IRAs" written by Natalie Choate.

unless it is for the sole lifetime benefit of a beneficiary who was chronically ill or disabled on the date of death of the Plan Participant.

The 2022 Proposed Regulations released two notable exceptions to the general rule that an Accumulation Trust qualifies for the 10-Year Rule (unless held for the sole lifetime benefit of a disabled or chronically ill beneficiary). Specifically, the Proposed Regulations introduce a new exception to this rule if there is a Designated Beneficiary who is a minor child of the Plan Participant. In this case, the Plan Participant is treated as having an Eligible Designated Beneficiary allowing life expectancy payments to be made until ten years after the year in which the child reaches age 21. The authors refer to this exception as the "Minor Child Accumulation Trust Exception."

The following examples from the Preamble illustrate this rule:

> [A Plan Participant] names a see-through trust as the sole beneficiary of the employee's interest in the plan, and the trust beneficiaries are the employee's surviving spouse and the employee's adult child who is not disabled or chronically ill, then the employee is treated as not having an eligible designated beneficiary. As a result, the employee's entire interest must be distributed no later than 10 years after the employee's death. However, if there is another designated beneficiary who is the employee's child and who, as of the date of the employee's death, has not yet reached the age of majority, then, under the exception described in the preceding paragraph, the employee is treated as having an eligible designated beneficiary. In [the situation described in the preceding sentence], if the trust is receiving annual distributions using the life expectancy rule, then a full distribution from the plan would not be required until ten years after the minor child reaches the age of majority.

Additionally, the Proposed Regulations allow for disregarding certain trust beneficiaries for the purposes of determining the Designated Beneficiary, even if a beneficiary's interest is not eliminated prior to the September 30th Designation Date. Specifically, a beneficiary of an Accumulation Trust can be disregarded when entitlement is conditioned upon the death of an individual who has not reached age 21 if the terms of the trust requires full distribution to such individual by the later of (1) the 10th calendar year following the calendar year of the Plan Participant's death, or (2) the end of the 10th calendar year following the calendar year in which that individual attains age 21. The authors refer to this exception as the "Age 31 Outright Distribution Accumulation Trust."

This Regulation is the recipient of Natalie Choate's "Best Proposed Regulation of the Year (2022) Award."

The following example from the Preamble illustrates this rule:

> [A]ssume an employee names a[n] [Accumulation] trust as the sole beneficiary, the trust permits specified amounts to be paid to the employee's niece until the niece reaches age 31 (age of majority plus 10 years) . . . . The trust is scheduled to terminate with a full distribution of all trust assets to the niece when the niece reaches age 31, but if the niece dies before this scheduled termination, then the amounts remaining in the trust will be paid to the employee's sibling. In that case, the only beneficiary designated under the plan for purposes of section 401(a)(9) and these regulations is the employee's niece because the employee's sibling is disregarded under the exception described in the preceding paragraph. However, if the see-through trust terms do not require a full distribution of amounts in the trust representing the employee's interest in the plan until the niece reaches age 35, then this exception does not apply, and both the employee's niece and sibling are treated as beneficiaries designated under the plan for purposes of section 401(a)(9) and these regulations.

As a result of the SECURE Act's 10-Year Rule, it was thought that trust drafters would no longer need to require that the Designated Beneficiary of an Accumulation Trust be the oldest Person who can benefit from the trust because the 10-Year Rule will apply in all events where there are multiple beneficiaries of an Accumulation Trust; however, the 2022 Proposed Regulations provide that if a Plan Participant dies after his or her Required Beginning Date then Required Minimum Distributions must occur in each of Years 1 through 9 based on the life expectancy of the oldest Designated Beneficiary. Therefore, trust drafters should make sure that beneficiaries who are older than the intended Designated Beneficiary cannot benefit in order to minimize Required Minimum Distributions in Years 1 through 9, although this is not as important as it was pre-SECURE due to the fact that all assets must be distributed from the IRA/Plan on or before December 31st of the tenth calendar year following the Plan Participant's death. Advisors must also be careful not to cause a Non-Person to be a Tier I or Tier II Beneficiary of an Accumulation Trust after the Designation Date, which would cause the Trust to not qualify as an Accumulation Trust resulting in the application of the 5-Year Rule (or the At-Least-As-Rapidly Rule).

Prior to the SECURE Act becoming effective on January 1, 2020, the Designated Beneficiary of an Accumulation Trust, for the purposes of the Required Minimum

Distribution rules, was the oldest individual beneficiary of the trust, even if such person is merely a contingent beneficiary. This is discussed further in Chapter 3, Section II. Any potential appointees under a power of appointment held by a trust beneficiary over property held under an Accumulation Trust are taken into account for the purposes of determining the Designated Beneficiary of the IRA/Plan. Therefore, for pre-SECURE Act trusts, no power of appointment should be exercisable in favor of individuals who are older than the desired Designated Beneficiary, or in favor of any Non-Person entities, because this would invalidate the ability to use the Designated Beneficiary's life expectancy for Required Minimum Distribution purposes.

For example, power of appointment language used before the SECURE Act (or used in a situation where it is anticipated that an Accumulation Trust will be established for the sole lifetime benefit of a disabled or chronically ill beneficiary) commonly would have been (or would be) limited as follows:

Notwithstanding the above, the holder of any power of appointment of any trust herein established which is the recipient of any IRA or pension plan distribution may not exercise such power of appointment in favor of any individual older than the applicable "Designated Beneficiary" or any entity that is not an individual.

Further, any appointee must be a descendant of the great-grandfathers and great-grandmothers of the Grantor of this Trust.

Accordingly, any Non-Person Tier I or Tier II Beneficiaries of a desired Accumulation Trust should be eliminated before the Designation Date (September 30th of the calendar year following date of death of Plan Participant) by full payment of the share of the trust otherwise allocable to them by such Non-Person Tier I or Tier II Beneficiaries by amendment of the trust by independent trust protectors or possibly by court order. Further, powers of appointment should have been trimmed back before the Designation Date and any powers held by the trustee or any other party (such as trust protectors) that would have allowed for the addition of Non-Person beneficiaries or individuals older than the Designated Beneficiary should have also been trimmed back as well, if desired or necessary to assure qualification as an Accumulation Trust prior to the SECURE ACT. Post SECURE Act and the Proposed Regulations discussed in Chapter 8 allow for much more flexibility with respect to powers of appointment by only taking into account the takers in default of an exercise as beneficiaries if the power if not otherwise exercised or modified prior to the Designation Date.

It is also possible to draft so that a conventional credit shelter trust or generation skipping trust can be the recipient of IRA/Plan benefits to be paid out over the lifetime of a Designated Beneficiary by having a separate "shadow trust" established under the trust instrument with identical dispositive provisions to the main trust, except that certain provisions are modified as necessary in order to result in the maximum deferral of IRA/Plan benefits. "Shadow Trust" provisions for pre-

SECURE Act Trusts would typically provide that only individuals younger than the Designated Beneficiary can receive benefits from the trust, and that appointees under any power of appointment must be individuals who were younger than the Designated Beneficiary. The non-IRA/Plan assets can be held, managed, and administered under the main trust provisions and would not be subject to the provisions of the separate Shadow Trust. This is no longer necessary for most "Stretch Trusts" under the SECURE Act, as discussed in Chapter 7.

Most lawyers who study the new SECURE Act will make changes to the trust language they use for Accumulation Trusts to take the above considerations and further issues discussed in Chapter 7 on the SECURE Act into account.

21. Conduit Trust. A trust that is the beneficiary of an IRA/Plan which requires that all distributions from the IRA/Plan must be paid to a specified Designated Beneficiary and does not authorize the trustee thereof to accumulate or withhold any distributions from the IRA/ Plan. The Required Beginning Date and Required Minimum Distribution rules will normally apply as if the Designated Beneficiary of the Conduit Trust is the sole direct beneficiary. Thus, all beneficiaries (other than the Designated Beneficiary) can be disregarded for the purpose of determining the Designated Beneficiary, and the Designated Beneficiary will be treated as the individual beneficiary for Required Minimum Distribution rule purposes. A Conduit Trust can thus have beneficiaries older than the desired Designated Beneficiary, and Non-Persons (such as charities) as beneficiaries. Moreover, unlimited power of appointment rights may be given to one or more individuals, so long as all distributions from the IRA/Plan to the trust are required to be paid to the Designated Beneficiary upon receipt from the IRA/Plan during his or her lifetime.

    Under most circumstances, the proceeds received by the Designated Beneficiary will not be protected from the creditors of the Designated Beneficiary, or from the federal estate tax at the Designated Beneficiary's death, because a Conduit Trust requires that he or she must receive all IRA/Plan distributions. However, a Conduit Trust may provide that a charity or another Non-Person may be a remainder beneficiary of the trust, and this will not jeopardize use of the desired Designated Beneficiary's life expectancy when the Life Expectancy Rule can apply.

    Under the SECURE Act, a Conduit Trust will only qualify for a lifetime payment when the Designated Beneficiary is the Plan Participant's Surviving Spouse, an individual no more than ten years younger than the Plan Participant, or a disabled or chronically ill beneficiary. A minor can qualify for Life Expectancy payments to be made until he or she reaches age 21, after which the 10-Year Rule will apply, so that there will be many irresponsible 28-year-olds receiving significant payments from Conduit Trusts by trustees who will have wished that an Accumulation Trust had been used despite the tax savings that may have been obtained through the use of a Conduit Trust.[67]

It might be possible to "toggle" a Conduit Trust into an Accumulation Trust within nine months after the death of the Plan Participant in most states, if the Designated Beneficiary who is to receive all distributions of IRA/Plan benefits per the trust instrument disclaims his or her right to receive mandatory distributions of all IRA/Plan payments, as further described in Chapter 7.

It may also be possible for a Trust Protector to hold an amendment power to "toggle" a Conduit Trust into an Accumulation Trust, however, the power must be exercised prior to the Designation Date.[68] A Trust Protector given this ability should also have the power to change remainder beneficiaries within nine months following the death of the Plan Participant as necessary to comply with the Designated Beneficiary Rule discussed in Paragraph 23 below. See PLR 200537044.

Conduit Trusts will be used much less frequently under the SECURE Act, because they will only have utility when established for a Surviving Spouse or an individual no more than 10 years younger than the deceased Plan Participant. Accumulation Trusts will still be usable for beneficiaries who are disabled or chronically ill on the date of the Plan Participant's death so that Conduit Trusts will not have to be used for them in order to be eligible for the Life Expectancy Rule.

22. QTIP Minimum Distribution Rules. When IRA/Plan benefits are payable to a QTIP trust that must pay all income to the Surviving Spouse to qualify for the estate tax marital deduction, Revenue Ruling 2006-26 requires that both (a) the Plan/IRA and the QTIP trust each make affirmative marital deduction elections; and (b) that the greater of the Required Minimum Distribution percentage or all income from within the plan must be paid to the QTIP trust annually. Further, the spouse must have the right to require that all income earned within the Plan be distributed to the QTIP Trust, and the normal QTIP Trust rules provided under Internal Revenue Code Section 2056 will apply. A QTIP trust will qualify as a Conduit Trust, and the Surviving Spouse will be considered to be the Designated Beneficiary thereof if the IRA/Plan meets the requirements set forth above. This is further discussed in Chapter 3, Section II (F) of this outline.

Note – A Surviving Spouse whose right to withdraw from the IRA/Plan is restricted will not be able to roll the IRA/Plan into his or her own IRA.[69]

23. Delay in Division Problem. What if the trust agreement or last will and testament of a Plan Participant who died before 2020 provided that a trust or trusts held for the Designated Beneficiary will not be separated until after an event which will not

[67] If the minor is the Designated Beneficiary of an Accumulation Trust, then all IRA/Plan assets need to be distributed based upon the 10-Year Rule instead of waiting until ten years after the individual has reached the age of majority.
[68] The September 30th of the calendar year following the date of death of the Plan Participant.
[69] Treas. Reg. § 1.408-8, A-5(a).

occur before the deadline for the establishment of separate accounts (December 31st of the calendar year following the Plan Participant's death).

For example, the applicable trust provides that the trustee is to "divide the assets equally into separate trusts for my children after my youngest child has reached age 25." Based on this language, if the Plan Participant died prior to January 1, 2020 each trust is going to have to take out Required Minimum Distributions over the life expectancy of the oldest child (assuming that the children and individuals younger than the oldest child are the only beneficiaries of the trusts that will be established).

A better approach would have been to provide for funding of a side trust that could be used to provide health, education, maintenance, and support for the youngest child or children, with the net remaining amount to be distributed equally among the trusts for the children once the youngest child has reached age 25. The IRA/Plans can then be allocated equally among the trusts for the children, which can be formed on or before the deadline for establishing separate accounts.

If the Plan Participant died on or after January 1, 2020, then the trust will likely be subject to the 10-Year Rule regardless of whether separate accounts are established, as discussed in more detail in Chapter 7.

24. Separate Accounts Rule. This rule allows an IRA/Plan to be paid to multiple beneficiaries based upon their respective life expectancies as if separate IRA/Plan accounts had been established for each separate Designated Beneficiary and applicable trust, and is now only relevant if the Plan Participant died prior to January 1, 2020, or if the IRA/Plan will benefit two or more Eligible Designated Beneficiaries who can separately qualify for use of the Life Expectancy Rule.

The applicable distribution period for each separate account is determined by disregarding the other beneficiaries, but only if the separate accounts are established on a date which is no later than December 31st on the calendar year following the year of the Plan Participant's death.[70] However, when IRA/Plan account creation occurs by division from a single trust that is named as beneficiary, the separate accounts rule is not available for purposes of determining the life expectancy of multiple beneficiaries.[71] Where the Plan/IRA beneficiary is a trust with multiple beneficiaries, the life expectancy of the oldest possible Designated Beneficiary is used to determine the applicable distribution period. The authors are hopeful that Final Treasury Regulations issued under the SECURE Act will not require that separately created trusts be the separate beneficiaries of IRA/Plan accounts to enable multiple Eligible Designated Beneficiaries to each have his or her life expectancy used.

[70] Treas. Reg. 1.401(a)(9)-8, A-2(a)(2).

[71] Treas. Reg. § 1.401(a)(9)-4, A-5(c).

Example:

Where an IRA is payable by beneficiary designation to a trust with three minor children of the Plan Participant, and after the death of the Plan Participant the IRA splits into three separate shares payable to each beneficiary, the Required Minimum Distribution Rules will apply under each separate share as if each beneficiary was the same age as the oldest beneficiary (PLR 200317041; PLR 200317043; PLR 200317044; PLR 200432027).

The application of the Separate Account Rule for trusts funded under IRA/Plans of Plan Participants who die after 2019 is uncertain when the IRA/Plan is paid in trust or outright to two or more Eligible Designated Beneficiaries who can qualify for the use of a Life Expectancy Rule but the authors believe that unless separate accounts or separate trusts are established as discussed below, the life expectancy of the oldest Eligible Designated Beneficiary will have to be used.

For example, if an IRA/Plan is left to a Plan Participant's revocable trust, which states that fifty percent (50%) of the IRA/Plan is to be devised to a Conduit Trust for the benefit of Child A, and fifty percent (50%) of the IRA/Plan is to be devised to a separate Conduit Trust for the benefit of Child B, it seems that the applicable distribution period for each Conduit Trust is determined based upon the age of Child A (the oldest Designated Beneficiary), and Child B cannot separately calculate the applicable distribution period based on his or her life expectancy.

25. Separate Trust Rule. This rule allows separate trusts that are funded from a single IRA/Plan to be considered as having been funded separately and will only apply in certain circumstances. This applies as long as the IRA/Plan is divided into separate IRA/Plans, with the applicable separate trust being named as the beneficiary of the corresponding separate IRA/Plan under the beneficiary designation.[72] Each trust (at the time it receives benefits) must be a separate trust under applicable state law with its own taxpayer identification number. If the Plan Participant died on or after January 1, 2020, then the Separate Trust Rule may still be applicable if the IRA/Plan is made payable to separate trusts for separate Eligible Designated Beneficiaries, as discussed in more detail in Chapter 7.

Example:

An IRA that is payable one-third to a trust for one minor child of the Plan Participant, one-third to a trust for another minor child of the Plan Participant, and one-third to a trust for an adult child of the Plan Participant will qualify to facilitate having the applicable distribution

[72] PLR 200537044 states that the separate trust rule will still apply if the IRA/Plan is not divided into separate IRAs/Plans, so long as the beneficiary designation specifies that a distinct portion of the IRA/Plan will be payable to each separate trust. The authors are not aware of any other IRS guidance on this issue. Some conservative planners may want to divide the IRA/Plan into separate IRA/Plans during the Plan Participant's lifetime to assure that the separate trust rule will apply.

period determined separately for each such trust, based upon the life expectancy of each minor child, and until each such minor child reaches adulthood. Note that this can have a much better result than what would apply in the example of the Separate Accounts Rule, especially if there is a large age difference between the beneficiaries of a trust.

26. Mistake Number 10. This is from the article entitled *Ten Common Portability Mistakes and What You Need to Know to Avoid Them* published February 1, 2016 on Leimberg Information Services by Alan Gassman, Ed Morrow, Seaver Brown and Brandon Ketron.

When Plan Participants run the math on different options for distributions, there is not as large a disparity between net after tax amounts received as one might think. See the chart below.

Example[73]

In the next scenario below, we assumed that a $1,000,000 IRA left by a Plan Participant who died before 2020 would grow at 6% per year for a 50-year-old Surviving Spouse. The Surviving Spouse had an IRS table's life expectancy of 35 years. We further assumed that any amount withdrawn would be saved and grow at an after- tax rate of 5.3% to compare the after-income tax values of the IRA, and that the after tax investments could be purchased with minimum payments after paying income taxes. We assumed that the IRA balance can be discounted by 30% to take into account that it will be 100% taxable when eventually distributed. We also assumed that the separate account funded with after income tax withdrawals would receive a fair market value income tax basis on the death of the Surviving Spouse so that there would be no tax on the unrealized depreciation, realizing appreciation.

Age	Rollover IRA	Conduit Deceased Spouse Under 70 ½	Conduit Deceased Spouse Over 70 ½	Accumulation IRA
50	$ 742,000	$ 742,000	$ 739,193	$ 739,193
55	$ 992,963	$ 992,963	$ 968,135	$ 967,998
60	$ 1,328,809	$ $1,328,809	$ 1,266,007	$ 1,261,663
65	$ 1,778,246	$ 1,778,246	$ 2,183,771	$ 2,110,098
70	$ 2,376,183	$ 2,374,035	$ 2,183,771	$ 2,110,098
75	$ 3,146,213	$ 3,124,402	$ 2,850,585	$ 2,704,510
80	$ 4,143,625	$ 4,082,442	$ 3,707,690	$ 3,440,920
85	$ 5,429,462	$ 5,304,717	$ 4,809,023	$ 4,381,034
90	$ 7,081,106	$ 6,869,367	$ 6,226,670	$ 5,671,900

[73] The numbers will be updated when the next edition of the book is released, which the authors anticipate to be shortly after the Proposed Regulations are finalized.

27. <u>When is a Roth IRA Withdrawal Subject to Income Tax?</u> – **<u>More often than one may think!</u>** The complicated labyrinth of IRA taxation and distribution rules does not stop in the area of Roth IRAs.

While the vast majority of Roth IRA distributions will never be subject to income tax, there are exceptions to this that can apply both to contributors and inheritors.

By definition, the question is whether a distribution is "non-qualified" or qualified?

Distributions that are "non-qualified" may be subject to tax, depending on the "investment in the contract," which is generally equivalent to the "tax basis."

In order to be considered a qualified distribution, two tests must be met:

The first test is that the distribution must be made after one of the following events occurs:

A. The Plan Participant reaches the age of 59½;

B. The Plan Participant's death;

C. The Plan Participant is totally disabled; or

D. The distribution is made for a "qualifying special purpose," including, but not limited to, distributions of up to $10,000 for the purchase of a first home, distributions for certain medical expenses, distributions of up to $5,000 for the birth or adoption of a child, and distributions to individuals who are called to active military duty.

The second test is that the distribution must be at least five years after the Plan Participant first makes a contribution to the Roth IRA. This applies for both the Plan Participant and a beneficiary. If a Plan Participant's waiting period is not satisfied prior to his or her death, then his or her waiting period will carry over to the Designated Beneficiary. The Designated Beneficiary must then wait the remaining number of years to satisfy the five-year waiting period requirement in order for his or her distributions to be "qualified distributions."

For example, Alex forms a Roth IRA in 2023, and dies in 2025 leaving his Roth IRA to his son, Ben. Ben cannot take "qualified" distributions from the inherited Roth IRA until the five-year test is satisfied on January 1, 2028. Since this is an inherited Roth IRA, Ben will be subject to the Required Minimum Distribution rules and any distribution period to the end of the five year waiting period will be considered a non-qualified distribution, but likely will be considered a non-taxable return of basis, as discussed in more detail below.

For purposes of calculating the five-year waiting period, the initial contribution is considered to have been made on January 1st of the year in which the first contribution was made. Subsequent contributions to a Roth IRA do not start a new five-year waiting period.

For example, if Alex contributed $1,000 to a Roth IRA on December 31, 2023, Alex could satisfy the five-year rule on December 31, 2027 due to the fact that the five-year period began on January 1, 2023. Further, even if Alex rolled over his IRA worth $80,000 into the Roth IRA in a year following his original contribution, the five-year waiting period will be considered to be satisfied on December 31, 2027.

If the distribution does not meet these two tests, then it is considered to be a "non-qualified" distribution with all income within the Roth IRA from its inception being taxed only after the principal has been paid out.

Non-qualified distributions are deemed to first come from the Plan Participant's "investment in the contract" or basis (i.e., the contributions the Plan Participant made during his or her lifetime), and then from income. In other words, distributions will not be taxable unless all previous contributions or amounts that have been rolled over from a traditional IRA have been distributed.

This is called being taxed on the "best first" basis.

Therefore, inherited Roth IRA distributions will rarely, if ever, be considered taxable. Even if the beneficiary inherited the Roth IRA prior to the five year test being satisfied, it is likely that there would be sufficient basis or investment in the contract to satisfy any Required Minimum Distributions that a beneficiary would be required to take in the years remaining to satisfy the five year waiting period. After the five-year period is satisfied, all distributions will be considered as "qualified" and not subject to tax, as discussed above.

Roth IRA distributions taken prior to age 59½ by the Plan Participant will be subject to the 10% excise tax unless one of the exceptions are met. Additionally, distributions may be subject to tax if the Roth IRA engages in a prohibited transaction.

28. Medicaid Planning with IRAs. In Florida, an unmarried long-term care Medicaid applicant can only have $2,000 of "countable" assets.

Certain assets are excluded, such as personal physical possessions, one vehicle of any value, and the client's qualified homestead, so long as the client has an intent to return and the qualified homestead is worth less than $636,000.

Retirement accounts, such as an IRA, will be an exempt asset if the account is in payout status. If the applicant is age 72 (or 70½ prior to January 1, 2020), then the applicant's IRA will be in payout status because the applicant is required to take Required Minimum Distributions from the IRA. If the applicant is between 59½ and 72 (or 70½ if prior to January 1, 2020), the IRA will be in payout status, if the applicant is taking distributions that are based on his or her life expectancy.

As of January 1, 2022, a Medicaid applicant in Florida cannot receive more than $2,523 of gross monthly income.

The distributions that the applicant receives from an IRA, even if the IRA is an exempt asset, will be counted as income received by the applicant. If the Required Minimum Distributions cause the applicant to have too much income to otherwise qualify for Medicaid, then he or she can form an irrevocable Qualified Income Trust, which is also known as a Miller Trust.

Every month, enough of the applicant's income will be deposited into the Qualified Income Trust so that the amount of his or her income that is not deposited into the trust does not exceed the $2,523 monthly income limit. Any income distributed from the Qualified Income Trust to the applicant will be counted as income received by him or her. After the applicant's death, Florida will have a lien on the assets remaining in the Qualified Income Trust equal to the amount of total medical assistance Florida paid on his or her behalf.

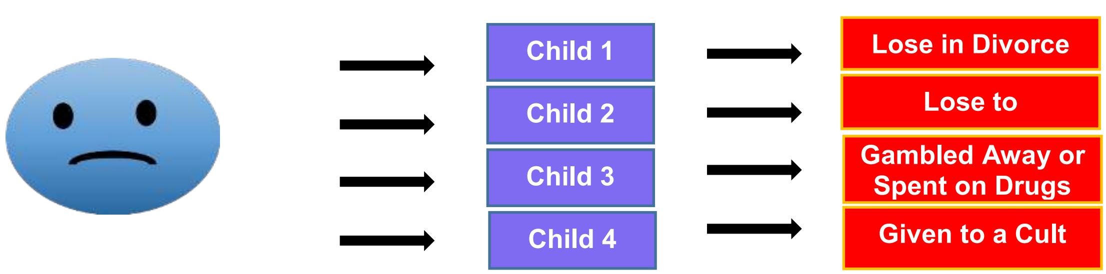
The money left in the applicant's IRA will pass pursuant to his or her beneficiary designation and will not be subject to any Medicaid liens.

29. Auto Switch. The name given to trust mechanisms that will automatically convert one kind of IRA/Plan beneficiary trust into another one. For example, if a Plan Participant signs a revocable trust that provides for three separate Accumulation Trusts to be established for her three separate adult children, the trust language may provide that if she dies with a minor child who was born after signing the document, then the Accumulation Trust that would have normally been opened and funded for the minor child would instead be a Conduit Trust to enable there to be a life expectancy payout until the minor child reaches age 21, so that the 10-Year Rule would apply thereafter. Toggling and Auto Switches are further discussed in Chapter 3, Section IV and Chapter 7, respectively.

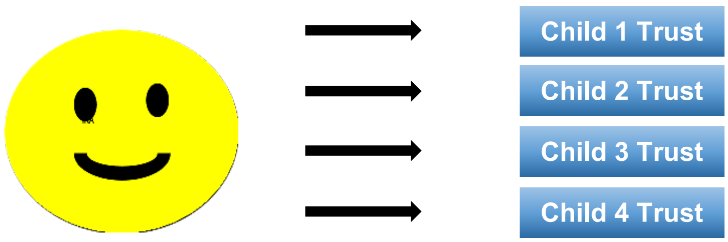
The following charts illustrate the application of the Required Minimum Distribution rules prior to passage of the SECURE Act (effective January 1, 2020). For charts that illustrate the application of the Minimum Distributions Rules after the passage of the SECURE Act, see Chapter 7.

ILLUSTRATION 2.13 – APPLICATION OF MINIMUM DISTRIBUTIONS RULES BEFORE PASSAGE OF THE SECURE ACT

Alternative #1 – (Directly to Each Child and Subsequently Lost?)

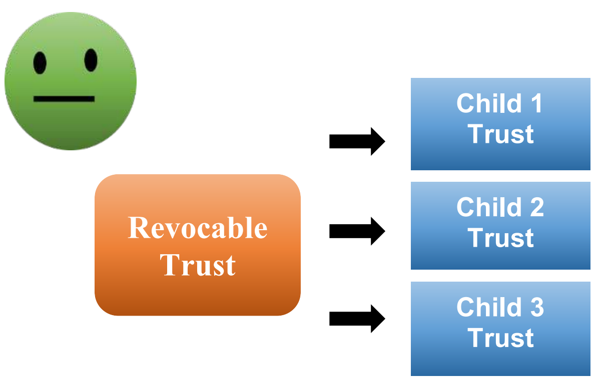


ALTERNATIVE #2 – (DIRECTLY TO SEPARATE TRUSTS FOR EACH CHILD)



If the trusts for the children are Conduit or Accumulation Trusts, then payments come out over the life expectancy of each child.

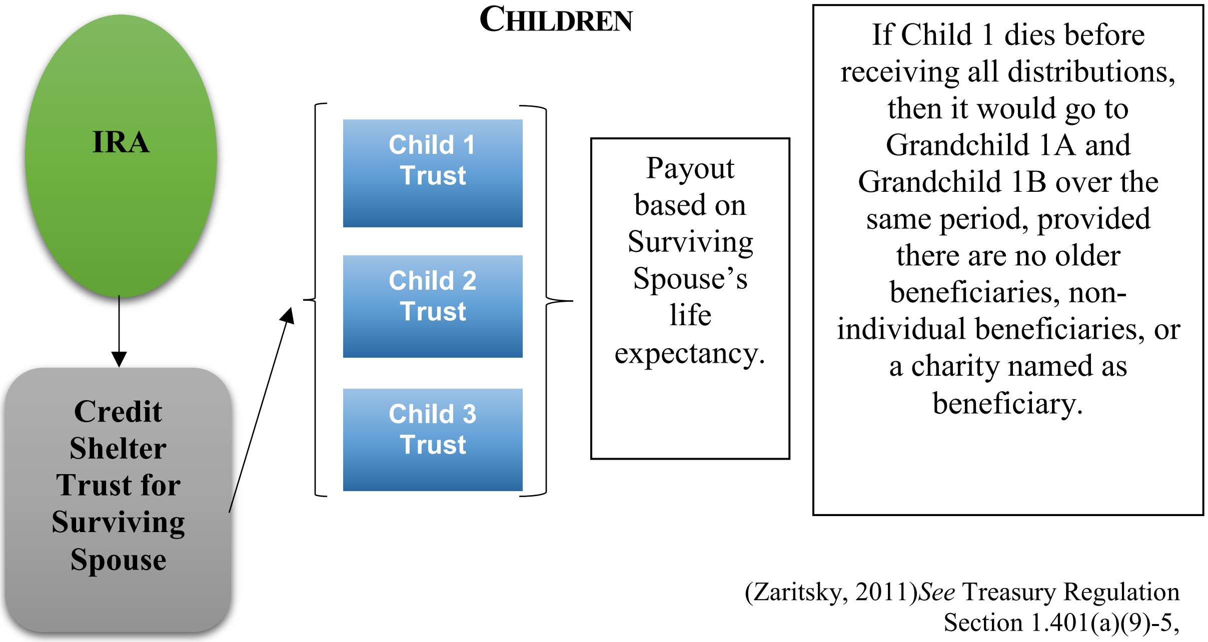
ALTERNATIVE #3 – (IRA PAYABLE TO REVOCABLE TRUST THAT IN TURN DIVIDES OR DIRECTS IRA BENEFICIARY RIGHTS TO SEPARATE TRUSTS FOR EACH CHILD)



PLRs 200317041, 200317044, 200432027-29 state that where an IRA is payable to a trust with multiple beneficiaries and splits into three separate shares payable to the beneficiaries under the terms of the trust document, the Required Minimum Distribution Rules will apply under each separate share as if each beneficiary is the same age as the oldest beneficiary.

NOTE: Where the IRA/Plan is payable directly to each separate trust, notwithstanding that each separate trust is established under a revocable trust, each beneficiary can use their respective life expectancy for Required Minimum Distribution

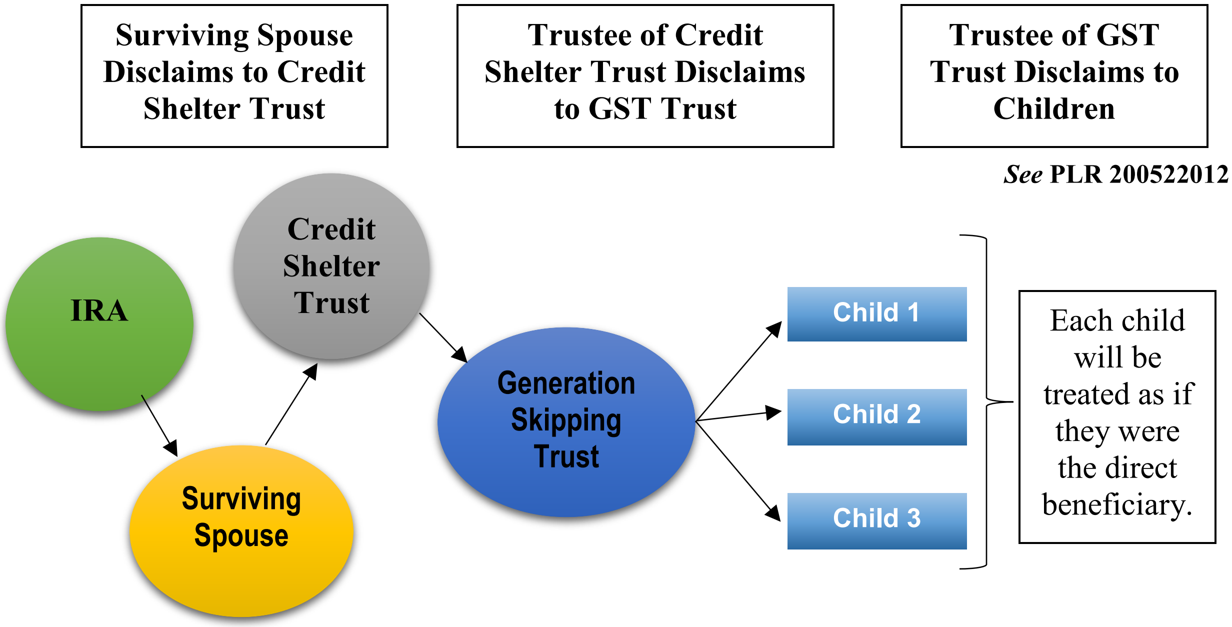
ALTERNATIVE #4 –
IRA TO CREDIT SHELTER TRUST AND SUBSEQUENTLY TO SEPARATE TRUSTS FOR CHILDREN



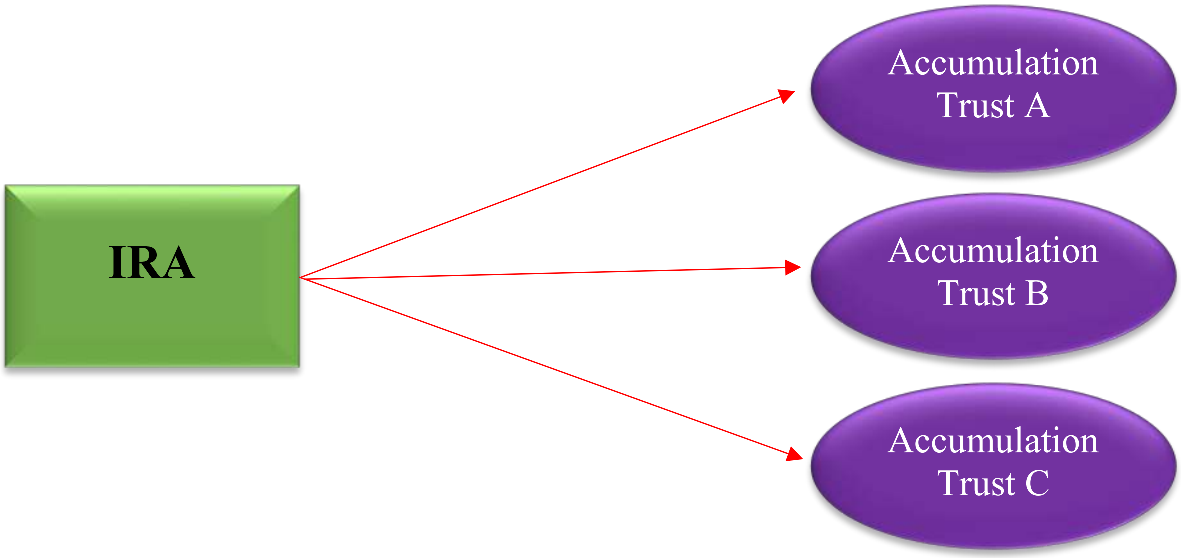
(Zaritsky, 2011)*See* Treasury Regulation Section 1.401(a)(9)-5, A-7(c)(3), Example 2

If Credit Shelter Trust is Conduit Trust, then no distribution is required until deceased spouse reaches age 70½ because the beneficiary of the Conduit Credit Shelter Trust is considered the "sole beneficiary."

ALTERNATIVE #5 – MULTIPLE DISCLAIMERS



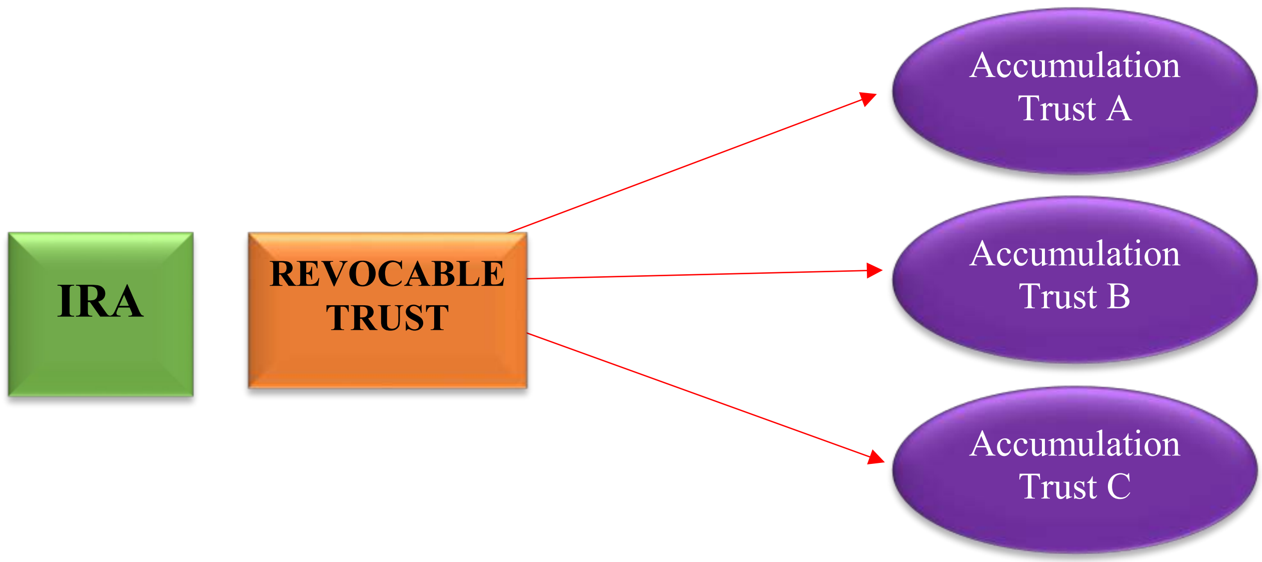
SCENARIO A –
IRA PAYABLE DIRECTLY TO PRE-EXISTING IRREVOCABLE ACCUMULATION TRUSTS



IRA goes directly one-third each to Accumulation Trust for Child A, Accumulation Trust for Child B, and Accumulation Trust for Child C.

Can use life expectancy of each of A, B, and C, if they are the Designated Beneficiary by September 30 following the date of death of Participant.

SCENARIO B –
IRA PAYABLE TO REVOCABLE TRUST WHICH IN TURN ESTABLISHES AND DIVIDES BETWEEN ACCUMULATION TRUSTS



IRA goes to Revocable Trust, which directs it one-third each into Accumulation Trust A, Accumulation Trust B, and Accumulation Trust C.

IF DONE WRONG
Only named beneficiary of the IRA is the Revocable Trust

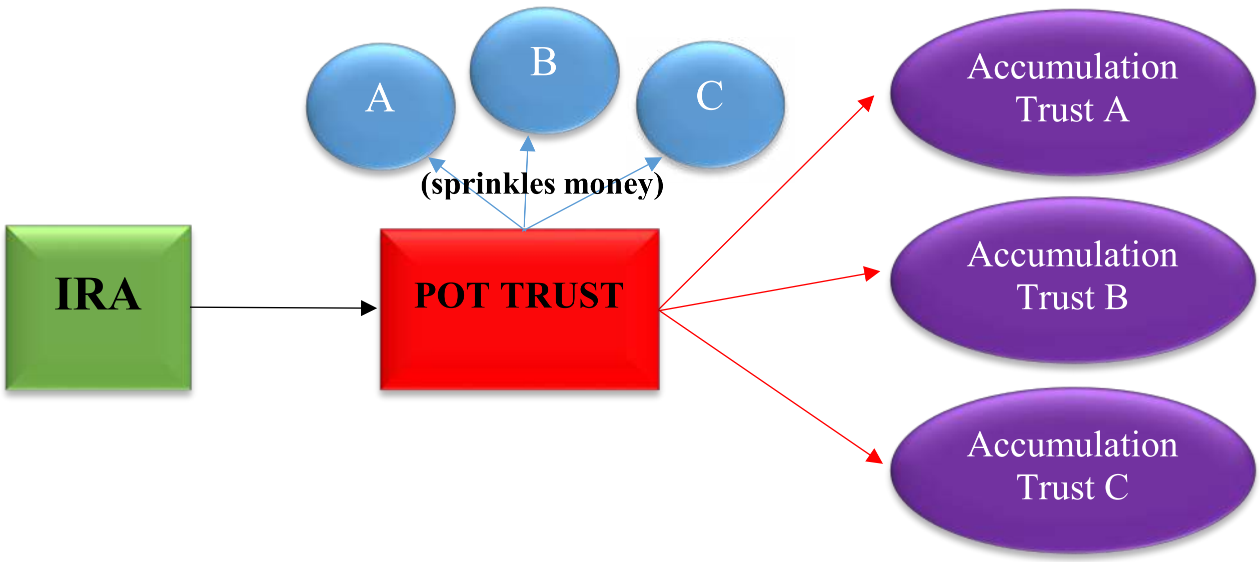
IF DONE RIGHT
IRA Beneficiary designation names the separate sub-trusts to be established under the Participant's Revocable Trust after death.

1. When IRA/Plan account division occurs by operation of a single trust that is named as beneficiary, the separate accounts rule is not available for purposes of determining the life expectancy of multiple beneficiaries.

2. Beneficiaries will use the life expectancy of the oldest beneficiary for Required Minimum Distribution Purposes. PLR 200317041, 200432027, 200432029.

3. Note – One PLR confirmed that if a single trust establishes each separate trust before receiving the inherited benefits, and each such to-be-established trust is the direct beneficiary of the retirement plan, the separate accounts rule can apply. Each beneficiary can use their respective life expectancy for Required Minimum Distribution Purposes. See PLR 200537044 and Choate 6.3.02(C) Drafting to achieve separate accounts under one trust instrument.

SCENARIO C – DON'T LET YOUR IRA GO TO POT, UNLESS THE POT TRUST IS DISTRIBUTED ON OR BEFORE SEPTEMBER 30 FOLLOWING THE DATE OF DEATH, FOLLOWING YEAR OF DEATH



IRA goes to POT Trust,* that sprinkles monies for A, B, and C and then divides into Accumulation Trust A, Accumulation Trust B, and Accumulation Trust C three years after death of beneficiary.

POT Trust may qualify as Accumulation Trust based upon the oldest of A, B, and C being the Designated Beneficiary – when divided later, the same payout (the oldest of A, B, and C) applies to all three parts.

Note – You can smile if the POT trust dissolves before September 30th in the year after the Plan Participant's death, or if all IRA beneficiary rights are transferred from the POT trust to separate trusts for each child on or before September 30th of the year after the Plan Participant's Death – Not so much POT.

**POT Trust is a trust held for multiple beneficiaries ("if you smoke pot, you probably will not get a distribution").*

CHAPTER 3 – PRE-SECURE ACT IRA AND PLAN BENEFITS PAYABLE TO TRUSTS

This Chapter covers the IRA "Stretch Trust Rules" as they applied, and will continue to apply, for situations where the Plan Participant died before 2020.

Chapter 7 covers the Post-SECURE Act Rules that apply when a Plan Participant has died after 2019, but the main differences are highlighted below:

PRE-SECURE ACT IRA AND PLAN BENEFITS PAYABLE TO TRUSTS

ITEM	PRE-2020 LAW	POST-2019 LAW
Required Beginning Date	Upon the later of: (a) April 1 of the calendar year following the year in which the Participant attains the age of 70½; or (b) April 1 of the calendar year following the year in which the Participant retires from employment, but only if the Participant is not a 5% owner of the stock of the employer or stock possessing more than 5% of the total combined voting power of all stock of the employer who sponsors the plan.	The reference to age 70½ has changed to 72 so that the Required Beginning Date is now the later of: (a) April 1 of the calendar year following the year in which the Participant attains the age of 72; or (b) April 1 of the calendar year following the year in which the Participant retires from employment, but only If the Participant is not a 5% owner of the stock of the employer or stock possessing more than 5% of the total combined voting power of all stock of the employer who sponsors the plan.
Life Expectancy Rule / 10-Year Rule	An individual beneficiary, or a trust that qualifies as a Conduit Trust or an Accumulation Trust, which is a beneficiary of any IRA/Plan qualifies for the Life Expectancy Rule (assuming that the IRA/Plan does not preclude application of Life Expectancy Rule). The Life Expectancy Rule allows Required Minimum Distributions to be made from the IRA/Plan over the life expectancy of the beneficiary (or a beneficiary of the trust).	In lieu of Life Expectancy Rule, the 10-Year Rule will apply where the IRA/Plan is left to an individual or to a trust that qualifies as a Conduit Trust or an Accumulation Trust. The 10-Year Rule requires that all assets be distributed from the IRA/Plan no later than December 31st of the 10th calendar year after the Plan Participant's death, and, under the Proposed Regulations, also requires that the beneficiary of the IRA/Plan take Required Minimum Distributions in years 1-9 following the Plan Participant's death if the Plan Participant died on or after his or her Required Beginning Date. Exceptions to this include IRA/Plans that are made payable to Eligible Designated Beneficiaries, to Conduit Trusts for the sole benefit of Eligible Designated Beneficiaries, or to certain Accumulation Trusts for the benefit of disabled or chronically ill Eligible

ITEM	PRE-2020 LAW	POST-2019 LAW
		Designated Beneficiaries or other beneficiaries where a minor is also a beneficiary under limited circumstances (defined below).
5-Year Rule /At-Least-As-Rapidly Rule	The default Required Minimum Distribution payout rule states that all assets must be distributed out of the IRA/Plan no later than December 31 of the year that is 5 years after the calendar year of the Plan Participant's death. An exception to this applies where the Plan Participant dies after reaching his or her Required Beginning Date, in which event the Required Minimum Distributions from the IRA/Plan can be paid over the life expectancy of the deceased Plan Participant based upon the deceased Plan Participant's age under the single life table, without annual recalculation of life expectancy.	This Rule has not changed.
Conduit Trust	A trust that is required to pay all amounts withdrawn from an IRA/Plan immediately to a Designated Beneficiary was usually permitted to take distributions over lifetime of Designated Beneficiary.	Now defined under the Proposed Regulations as a See-Through Trust which provides that all distributions from the IRA /Plan will be paid to or for the benefit of specified beneficiaries upon receipt by the trustee. The rules regarding qualification of a Conduit Trust continue to apply, but the 10-Year Rule will apply in lieu of the Life Expectancy Rule unless the Designated Beneficiary of the Conduit Trust is an Eligible Designated Beneficiary. Additionally, the law continues to treat the Designated Beneficiary of a Conduit Trust as if he or she inherited the IRA/Plan directly.
Accumulation Trust	A trust that permits a Trustee to accumulate distributions from the IRA/Plan, and also qualifies to be considered as a "See-Through Trust" whereby the IRS will look to a beneficiary of the Trust as the Designated Beneficiary of the IRA/Plan for the purposes of	Now defined under the Proposed Regulations as a See-Through Trust that is not a Conduit Trust. The rule regarding qualification of an Accumulation Trust continues to apply, but the 10-Year Rule will apply in lieu of the Life Expectancy Rule unless the sole lifetime beneficiary of the Trust is a chronically ill or disabled Eligible Designated Beneficiary, or

ITEM	PRE-2020 LAW	POST-2019 LAW
	determining the Required Minimum Distribution payout. Would usually be treated the same as a Conduit Trust to allow lifetime annual distributions, not annually recalculated.	in certain limited circumstances where an Accumulation Trust benefits only Eligible Designated Beneficiaries during their lifetimes. Nevertheless, an Accumulation Trust can be used to have the 10-Year Rule apply instead of the 5-Year Rule or At-Least-As-Rapidly Rule (the Ghost Life Expectancy Rule).
Inherited IRA	After IRA/Plan Participant dies, beneficiary maintains the IRA and it is designated as an "Inherited IRA," then Life Expectancy Payout can apply without penalties for withdrawal if beneficiary is under 59½, but lifetime distributions must begin in the year after the year of death of the Participant (unless the Surviving Spouse is the sole beneficiary, in which event the distributions can be postponed until the Surviving Spouse reaches his or her Required Beginning Date).	Same Rule applies, except that the Life Expectancy Rule is available only if an Eligible Designated Beneficiary is the sole beneficiary of the inherited IRA. If an Eligible Designated Beneficiary is not the sole beneficiary of the Inherited IRA, then the 10-Year Rule applies in lieu of the Life Expectancy Rule.
Eligible Designated Beneficiaries (EDBs)	Did not exist under prior law.	Certain beneficiaries are afforded the ability to have a Life Expectancy Rule apply in lieu of the 10-Year Rule. There are five beneficiaries who are considered as Eligible Designated Beneficiaries, but they have varying rights which are briefly summarized as follows: (1) <u>Surviving Spouse</u> – may roll over or use Inherited IRA and withdraw over Life Expectancy, with annual recalculation, as under past law. May be inherited outright to child or under Conduit Trust to have the above deferral. (2) <u>Minor Child of Deceased Plan Participant</u> (but not a minor grandchild or any other minor), if inherits from the Inherited IRA of Surviving Spouse, 10-Year Rule applies. If a minor child inherits from IRA or Rollover IRA of either parent, then withdrawal each year based on Life Expectancy until Age of Majority, then 10-Year Rule applies. May be inherited outright to child or under Conduit Trust to have the above deferral.

ITEM	PRE-2020 LAW	POST-2019 LAW
		(3) <u>Disabled Beneficiaries</u> – may use Life Expectancy Rule if IRA/Plan is left to such beneficiary directly, to a Conduit Trust for the beneficiary's benefit, or to an Accumulation Trust for the beneficiary's sole benefit. If the IRA/Plan is left to an Accumulation Trust that is not for the sole benefit of such beneficiary, then the 10-Year Rule applies. (4) <u>Chronically Ill Individuals</u> – Same as Disabled Beneficiaries above. (5) <u>Beneficiary Less Than 10 Years Younger Than Plan Participant</u> – May use Life Expectancy if IRA/Plan is payable directly to such beneficiary or to a Conduit Trust for such beneficiary. The 10-Year Rule applies if the IRA/Plan is left to an Accumulation Trust. NOTE: If the Plan Participant dies after reaching his or her Required Beginning Date, then any beneficiary can use the At-Least-As-Rapidly Rule to choose to withdraw Required Minimum Distributions over the life expectancy of the deceased Plan Participant based upon his or her life expectancy under the Single Life Table, without annual recalculation.

It is important to remember that many of the rules applicable in this area are derived from Private Letter Rulings that are only binding on the party that requested the ruling, and a number of Private Letter Rulings in this area have been criticized by commentators for being inaccurate. However, Howard M. Zaritksy's "The Year in Review" annual write-up for Bloomberg/ BNA, Tax Management Estates, Gifts &Trusts Journal, includes the following discussion of the precedential value of Private Letter Rulings in Footnote #2:

Private Letter Rulings (PLRs) and technical advice memoranda (TAMs) are not legal precedents. §6110(k)(3). They may, however, show how the Service might address a similar case, and they have been cited and discussed by several courts. See, e.g., Wolpaw v. Commissioner, 47 F.3d 787 (6th Cir. 1995), rev'g T.C. Memo 1993-322 (taxpayers can rely on 20-year-old PLR, absent definitive regulations); Estate of Blackford v. Commissioner, 77 T.C. 1246 (1981) (noting that the Service litigation position was contrary to a prior PLR); Xerox Corp. v. United States, 656

F.2d 659 (Ct. Cl. 1981) (stating that PLRs are useful in ascertaining the scope of the doctrine adopted by the Service and demonstrating its continued and consistent application by the Service); Fanning v. United States, 568 F. Supp. 823 (E.D. Wash. 1983) (noting that a distinction between the facts of the instant case and those of prior cases had been cited in a TAM, and that TAMs are often relied upon by the courts).

Illustration 3.1 is a summary of which rules apply to each kind of See-Through Trust, and then the rules that apply prior to January 1, 2020 are explained in further detail below. For a similar chart that applies after January 1, 2020, see Chapter 7.

ILLUSTRATION 3.1
THE 15 RULES THAT APPLY TO SEE-THROUGH TRUSTS PRE-SECURE ACT

(Choate, Making Retirement Benefits Payable to Trusts, 2015) Apply to Both Accumulation and Conduit Trusts	Apply Only to Accumulation Trusts	Apply Only to Conduit Trusts
Any Accumulation or Conduit Trust must meet the following requirements in order for the stretch rules to apply:		
A. The Trust must be valid under state law.	A. Powers of Appointment must be limited only to certain appointees.	A. All distributions from the IRA/Plan must be paid to the trust beneficiary upon receipt by the Trustee.
B. The trust must be irrevocable (at least immediately after the death of the Plan Participant).	B. Permit Powers of Appointment only in favor of individuals who are younger than the Designated Beneficiary of any Accumulation Trust.	B. Remainder beneficiaries do not county for Required Minimum Distribution purposes.
C. The beneficiaries of the trust must be identifiable by being named, or by being members of, a class of beneficiaries that makes each power of attorney	C. Programming for tax efficiency as between GST and Non-GST Trusts.	C. All distributions from the IRA/Plan can pay trust expenses.
D. Only Beneficiaries on the Designation Date (September 30 of the year after the Plan Participant's death) county.	D. Contingent Beneficiaries count for Required Minimum Distribution purposes.	
E. Information must be provided to the Plan Administrator by October 31 of the year after the year of the Plan Participant's death.	E. Prevent the adoption or addition of an older beneficiary.	
F. Deceased beneficiary exemption.		

(Choate, Making Retirement Benefits Payable to Trusts, 2015) Apply to Both Accumulation and Conduit Trusts	Apply Only to Accumulation Trusts	Apply Only to Conduit Trusts
G. Special QTIP Marital Deduction Rules		

I. Rules That Apply To All See-Through (Both Accumulation and Conduit) Trusts

A. The trust must be valid under state law.

B. The trust must be irrevocable, at least immediately after the death of the Plan Participant.

C. The beneficiaries of the trust must be identifiable by being named, or by being members of a class of beneficiaries that makes each person identifiable.

D. Only Beneficiaries on the Designation Date count.

Trust beneficiaries who are no longer entitled to receive any benefit on the Designation Date (for example by disclaimer, removal by court order, or satisfaction of all bequests by September 30th of the calendar year following the year of Plan Participant's death) will not be counted for Required Minimum Distribution purposes. Only those beneficiaries present on the Designation Date are considered in determining the Designated Beneficiary.

E. Information Must Be Provided to the Plan Administrator by October 31st of the Year After the Calendar Year of the Plan Participant's Death.

The IRA/Plan administrator must receive appropriate trust documentation by October 31st of the next calendar year following the year of the Plan Participant's death. This will normally be accomplished by providing the IRA/Plan administrator with a copy of the actual trust document. Alternatively, the trustee of the trust can provide the IRA/Plan Administrator with a final list of all beneficiaries of the trust as of the Designation Date, and a certification by the trustee that all requirements necessary for the trust to qualify as a See-Through Trust have been met.

F. Deceased Beneficiary Rule. A beneficiary who survived the Plan Participant but does not survive to the Designation Date (September 30th following the death of the Plan Participant) is still considered to be as a beneficiary of the trust for Required Minimum Distribution purposes, unless the deceased beneficiary (or his successor in interest) has received full payment or has executed a valid disclaimer of all of such beneficiary's interests in the IRA/Plan or trust receiving the IRA/Plan before the Designation Date.

Notwithstanding the above, there may be situations where meeting the applicable See- Through Trust requirements is not as important. For example, if the Plan Participant died on or after January 1, 2020 and after his or her Required Beginning Date, it may be beneficial to intentionally not qualify the trust as a See-Through Trust if the deceased Plan Participant's life expectancy is greater than ten years so that the deceased Plan Participant's life expectancy can continue to be used under the At-Least-As-Rapidly Rule, as described in Chapter 7.

Further, if the Plan Participant died prior to January 1, 2020 and the oldest trust beneficiary is the same age or older than the Plan Participant, then See-Through Trust qualification will not result in a longer applicable distribution period, and the applicable distribution period will be the same if the trust satisfies the See-Through Trust requirements (the longer of the life expectancy of the Plan Participant or the life expectancy of the oldest trust beneficiary) will apply if the trust did not satisfy the See-Through Trust rules (the life expectancy of the Plan Participant).[74]

For example, if Al died in 2018 at age 75 and left his IRA to an Accumulation Trust for his older sister, Betty, then the applicable distribution period of the IRA would have been based upon Al's life expectancy (because he was younger than Betty). Therefore, it is not important whether the trust qualifies as an Accumulation Trust, because Betty's life expectancy will not need to be used in the situation where Al, as the Plan Participant, died after reaching his Required Beginning Date, and was younger than Betty.

II. Pre-Secure Act Rules That Apply To Accumulation Trusts Only

A. Powers of Appointment Must Be Limited For Pre-SECURE Act Accounts

As discussed in Chapter 8, the Proposed Regulations issued in 2022 on the SECURE Act provided much more defined rules for identifying which beneficiaries will be taken into account in determining the payout rules when an IRA/Plan is made payable to a See-Through Trust and a power of appointment exists. The following is a discussion of the rules that applied prior to the issuance of the Proposed Regulations and for IRA/Plans that must apply the pre SECURE Act rules.

Specialized drafting was required for powers of appointment held by beneficiaries of an Accumulation Trust (although the issuance of the February 2022 Proposed Regulations largely eliminated the importance of such specialized drafting). Before the issuance of the 2022 Proposed Regulations, it was understood that holders of powers of appointment over trusts who were the recipients of IRA/Plan assets should not have the power to appoint the IRA/Plan assets to or for the benefit of any individual (including spouses) older than the Designated Beneficiary, or to or for the benefit of any Non- Person, or the power to appoint or transfer assets to

[74] Choate's *The 201 Best and Worst* at 3-100.

another trust that could have individuals older than the Designated Beneficiary or a Non- Person as a beneficiary.

The need to limit powers of appointment so that assets cannot be appointed to older beneficiaries is generally not applicable if the Plan Participant died on or after January 1, 2020 due to the replacement of the Life Expectancy Rule with the 10-Year Rule under the SECURE Act (and also due to the 2022 Proposed Regulations relaxing the rules for determining the Designated Beneficiary where powers of appointment exist under a trust that holds an IRA/Plan). This is discussed in more detail in Chapters 7 and 8. Nevertheless, post- SECURE Act powers of appointment should be drafted to preclude the appointment of IRA/Plan assets to or for the benefit of a Non-Person, as the 10-Year Rule (or Life Expectancy Rule, if applicable) will not apply in lieu of the default 5-Year Rule (or possibly the At-Least-As-Rapidly Rule, if the Plan Participant died after reaching his or her Required Beginning Date) if a Non-Person is a beneficiary of the trust after the Designation Date (September 30th of the calendar year following the date of death).

B. Permit Powers of Appointment Only in Favor of Individuals – For Pre-SECURE Act Accounts, Such Individuals Must Be Younger Than the Designated Beneficiary of Any Accumulation Trust.

Most commentators believe that it is safe to allow the power of appointment to be exercisable in favor of any living individual younger than the Designated Beneficiary, while one or more conservative commentators believe that the powers should only be exercisable in favor of a limited class of individuals, such as descendants of the grandparents of the Plan Participant who are younger than the Plan Participant. This is because the Treasury Regulations state that a power of appointment can only be exercisable in favor of “individuals identifiable from the trust document.”[75]

The 2022 Proposed Regulations confirm that all of the beneficiaries of a See-Through Trust must be identifiable by September 30th of the calendar year following the calendar year of the plan participant’s death, and that a trust will satisfy the identifiability requirement “if it is possible to identify each person eligible to receive a portion of . . . the plan through the trust.” Previously, the presence of a power of appointment was considered to frustrate such requirement because the failure of the person who holds the power of appointment to exercise or restrict such power results in the inability to determine who the beneficiaries are. The Proposed Regulations provide a safe harbor with respect to the exercise or restriction of a power of appointment, which is further discussed in detail in Chapter 8.

The safe harbor under the 2022 Proposed Regulations provides that a See-Through Trust will not fail the identifiability requirement due to the presence of an

[75] Reg. §1.401(a)(9)-4, A-5 and A-6.

unexercised power of appointment or an exercised power of appointment after the date of death of the Plan Participant.

Oftentimes, planners provide beneficiaries with powers of appointment that can be exercised in favor of creditors of the power holder's estate to avoid imposition of federal generation skipping tax. Because a creditor of the power holder's estate could be a Non-Person, or a person older than the Designated Beneficiary, this will cause problems in qualifying the trust as a See-Through Trust. The clause can be drafted to provide that the power is exercisable only in favor of individual creditors of the estate who are younger than the otherwise applicable Designated Beneficiary.[76]

Conservative planners who believe that only "individuals identifiable from the trust document" who are younger than the Designated Beneficiary may be named as possible appointees can assure avoidance of imposition of generation-skipping tax by giving a non-skip beneficiary the power to withdraw trust principal, which may be subject to approval of an independent trustee, trust protectors, or other non-adverse parties. This power can achieve the same generation skipping tax avoidance results as the use of a power of appointment exercisable in favor of individual creditors of the estate of the power holder.

Nevertheless, as a result of the SECURE Act eliminating the "stretch" where IRA/Plan benefits are made payable to an Accumulation Trust in nearly all cases, restricting the class of appointees under a power of appointment only to individuals younger than the otherwise applicable Designated Beneficiary is currently important in two situations: (1) Where a Plan Participant has died before January 1, 2020, and an IRA/Plan is payable to an Accumulation Trust; or (2) Where a Plan Participant dies on or after January 1, 2020 and an IRA/Plan is made payable to an Accumulation Trust for the sole lifetime benefit of a Disabled or Chronically Ill beneficiary.

C. The Distributable Net Income Trap. As defined in Chapter 2, a separately taxable trust which receives distributions from an IRA will be subject to tax, except to the extent that it pays deductible expenses, which may include payments to charities that will qualify for the deduction under Section 642(c), as discussed in Chapter 5, and to the extent that it makes distributions which carry out "distributable net income" as described in Chapter 6. There are situations where an IRA/Plan distribution to a trust will cause the income to be "trapped" at the trust level, notwithstanding that distributions have been made from the trust which may equal or exceed the IRA/Plan distributions received. It is vitally important that Accumulation Trust documents have the proper language to assure that distributions made from the trust by the trustee will carry out distributable net income.

[76] PLR 200235038 - 200235041 and Robert S. Keebler, CPA *New IRS Ruling Validates the "IRA Inheritance Trust™."*

D. Programming for Tax Efficiency as Between GST and Non-GST Trusts.

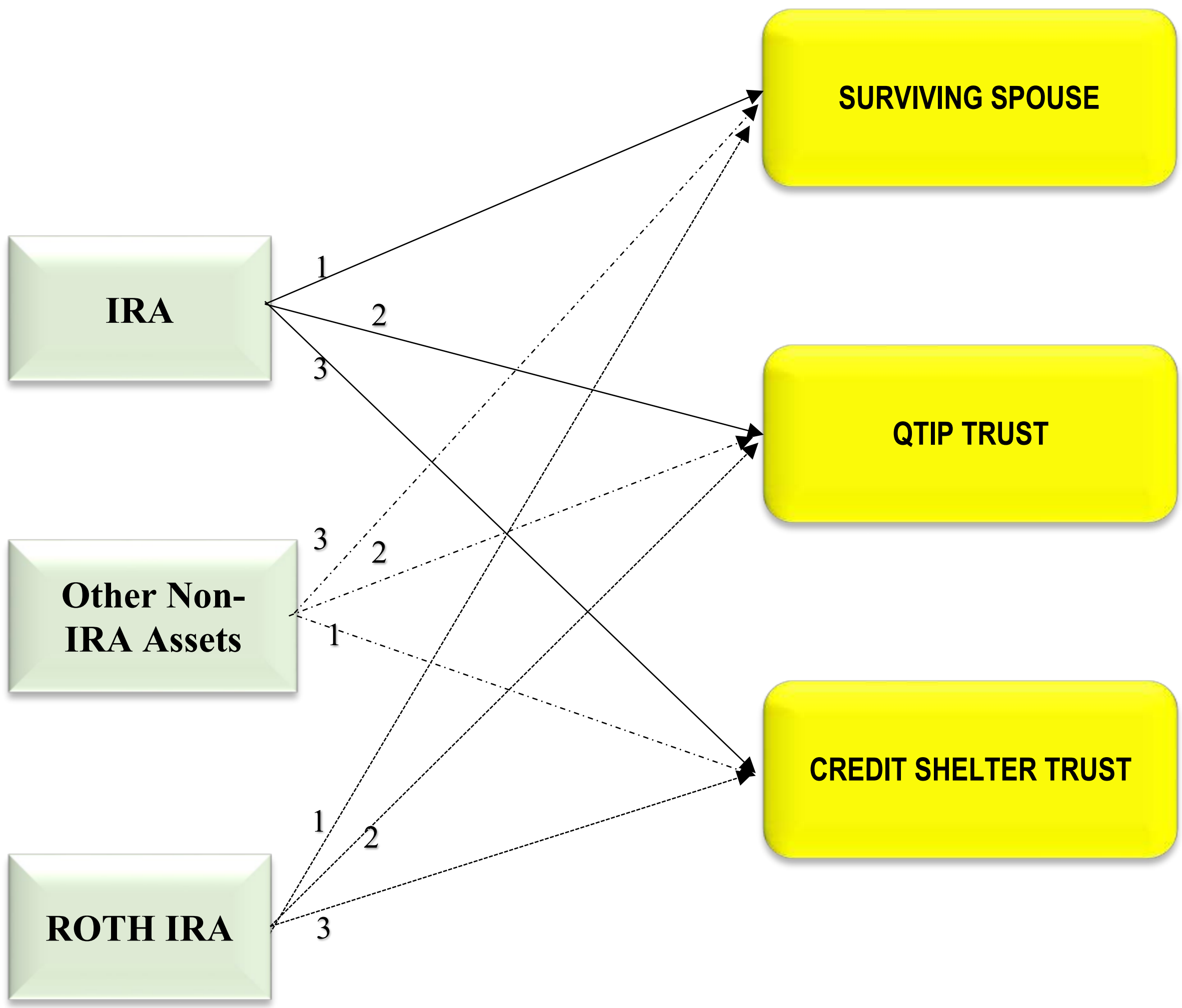
Where trusts are to be divided into generation skipping and non-generation skipping trusts for generation skipping transfer tax planning purposes, it will make sense to have a non- Roth IRA/Plan payable to the non-generation skipping trust so that the generation skipping trust will be funded with less built-in taxable income than is inherent with IRA/Plans in order to accumulate more wealth for subsequent generations. For example, if John dies in 2022 unmarried with a $2,500,000 IRA and $11,160,000 of other assets, he can leave $12,060,000 to a trust that will benefit his children without being taxed in their estate, and another $1,600,000 to a non-GST trust that has to be considered as owned by one or more of the children for estate tax purposes when they die. It seems to make sense to first allocate the IRA/Plan to the non-GST trust so that John's GST exemption is not used on assets that will incur income tax at ordinary income rates in the future (with no opportunity for a step-up in basis). Additionally, the formula to be used to define the assets that pass to the non-GST trust should be a fractional formula, and not a pecuniary bequest, because the use of an IRA/Plan to satisfy a pecuniary bequest may trigger tax upon funding. Nevertheless, the fractional formula can be drafted to allow the trustee of the trust to "pick and choose" assets to satisfy the devises to the respective beneficiaries or subtrusts so that the IRA/Plan can be allocated in the most tax-efficient manner.

The opposite rationale applies where a Roth IRA/Plan exists because of the tax advantaged status of a Roth IRA/Plan – there is no income tax payable on withdrawals from a Roth IRA. Therefore Roth IRA/Plan benefits would be allocated first to the GST Trust and then secondly to the non-GST Trust. See Illustration 3.2 below.

Language that may be used in a Trust Agreement to facilitate the above can be found in Appendix B.

Illustration 3.2 – Presumption of Order of Funding Between Surviving Spouse, QTIP Trust, and Credit Shelter Trust

Typically, the most tax efficient assets should be allocated to the bottom-most category, and the least tax efficient assets should be allocated to the uppermost category, except that a Non-Roth IRA would go to the Surviving Spouse.

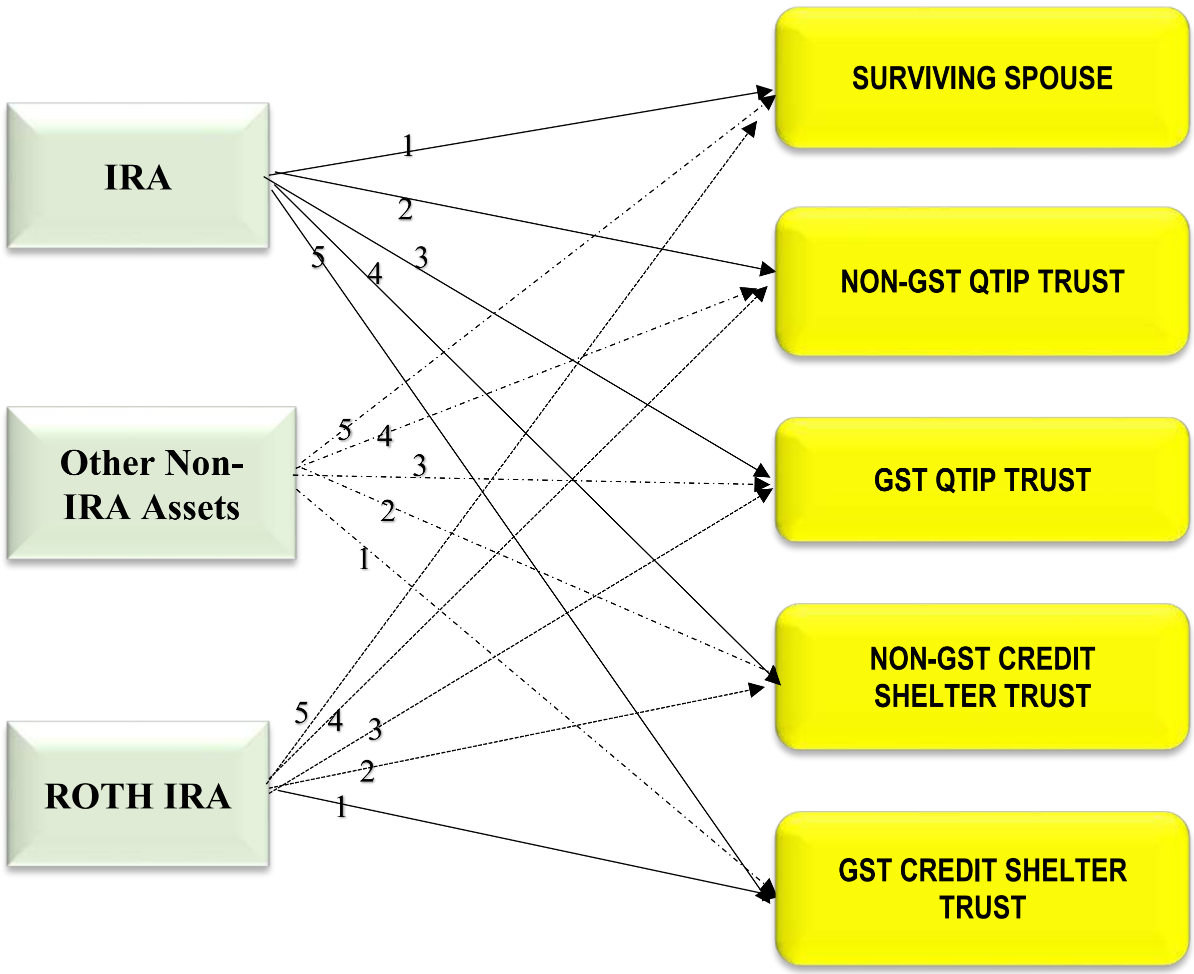


1. Roth IRAs allocated first to Credit Shelter Trust shares, and second to any QTIP Trust share.

2. Non-IRA (other than Roth IRA) assets that are not "income in respect of decedent" assets to pass first to QTIP share, then to Credit Shelter Trust share.

PRESUMPTION OF ORDER OF FUNDING BETWEEN SURVIVING SPOUSE, QTIP TRUST AND CREDIT SHELTER TRUST, BUT ASSUME NON-GST AND GST QTIP AND CREDIT SHELTER TRUSTS

Typically, the most tax efficient assets should be allocated to the bottom-most category, and the least tax efficient assets should be allocated to the upper-most category, except that a Non-Roth IRA would go to the Surviving Spouse.



Where IRAs are used to fund QTIP Trusts and Credit Shelter Trusts with or without other assets, the following rules of priority apply for income tax efficiency purposes:

1. Roth IRAs allocated first to GST Credit Shelter Trust shares, second to Non-GST Credit Shelter Trust Shares, third to any GST QTIP Trust share, and fourth to any Non-GST QTIP Trust Share.

2. Non-IRA (other than Roth IRA) assets that are not "Income in Respect of Decedent" assets to pass first to Non-GST QTIP share, second to GST QTIP share,

E. Contingent Beneficiaries Count for Required Minimum Distribution Purposes.

Even contingent distribution provisions that would only apply if no named beneficiary under an Accumulation Trust survives could conceivably be problematic. Following the passage of the SECURE Act, the concern is less pronounced because the ages of the beneficiaries of an Accumulation Trust do not affect the applicable distribution period under the 10-Year Rule that applies in virtually all situations where the IRA/Plan is left to an Accumulation Trust.[77] Nevertheless, there is still the issue of whether the estate of a descendant or a governmental entity would be considered to be a beneficiary of the trust, which would prevent qualification as a See-Through Trust.

Further, the 2022 Proposed Regulations provide additional clarity by allowing for certain beneficiaries to be disregarded, as discussed in more detail in Chapter 8. The following is a discussion of the rules and concerns that applied prior to the issuance of the Proposed Regulations, which is still relevant for IRA/Plans that must comply with the Pre-SECURE Act rules.

There is support for the proposition that having applicable intestacy rules apply will be safe. However, when read literally, the rules may require use of the life expectancy of the oldest individual who might inherit under the intestacy statute.

This issue has been addressed by several commentators. For example, Marcia Chadwick Holt, in her book entitled Estate Planning for Retirement indicates as follows:

Identifiable beneficiaries exclude an individual to whom [retirement benefits pass] under applicable intestate state law unless such individual is designated as provided above.[78]

The IRS does not recognize that state law provides for contingent beneficiaries – including escheat to the state – when a trust has no named beneficiaries. The IRS seems to be fixated on who the Plan Participant actually names as beneficiaries. The current PLRs do not require that a Plan Participant take into account beneficiaries that might inherit under state law.

Further, PLR 201320021 held that an IRA owner’s child was the only Designated Beneficiary under her IRA despite the fact that if the child died with no descendants and did not exercise his power of appointment, the IRA would pass to the IRA owner’s mother or brother under applicable state intestacy laws.

If the Private Letter Ruling and Marcia Chadwick Holt are correct, then the Accumulation Trust can provide that “if the Designated Beneficiary does not survive me, and does not leave descendants, then all remaining assets will be

[77] The sole exception is an Accumulation Trust for the sole lifetime benefit of a Disabled or Chronically Ill beneficiary, where the Life Expectancy Rule can apply based upon the age of such beneficiary.

[78] Treas. Reg. § 1.401(a)(9-4), A-1.

distributed based upon the intestacy rules of the State of [Plan Participant's domicile] that would apply to my estate if I died intestate" as opposed to "if none of my descendants survive, then pay outright to the descendants of my grandparents, per stirpes." The second alternative would cause the life expectancy of the oldest descendant of the Plan Participant's grandparents to apply for Required Minimum Distribution purposes, even if the Plan Participant has surviving descendants.

For pre-SECURE Act trusts, it is safest to limit the individuals who can inherit under the otherwise applicable intestacy laws to those who are younger than the Designated Beneficiary. For example, the Accumulation Trust can provide that "if the Designated Beneficiary does not survive me and does not leave descendants, then all remaining assets will be distributed based upon the intestacy rules of the State of [ ] that would apply to my estate if I died intestate, provided that any such heirs at law who are older than the Designated Beneficiary shall be considered to have died the day before the death of the Designated Beneficiary, which triggers application of such intestacy rules."

As a further example for pre-SECURE Act trusts, if the client wants to use "descendants of my grandparents" language, then the provision can be carved out to instead read "to the descendants of my grandparents, per stirpes, who are born after the date of birth of the Designated Beneficiary who is a beneficiary of any trust herein established which receives retirement plan benefits, any distributions therefrom, or the right to receive distributions therefrom."

Planners can also draft the trust to give independent trust protectors or trustees the ability to modify the trust language on or before September 30th of the calendar year following the calendar year of the Plan Participant's death. While it is not clear whether any such modifications will be respected by the IRS, there may be further guidance between now and when a client a dies, so language that clearly points out the need for trustees and trust protectors to address this issue without delay after the death of the IRA/Plan Participant or beneficiary can be important.

A Private Letter Ruling is not binding on the IRS except with respect to the Plan Participant who requests it. Therefore, other commentators believe that it is best to take the more conservative approach of naming a contingent beneficiary who is now living that will receive the IRA/Plan outright and immediately after the death of one or more prior beneficiaries. If there is a beneficiary that will receive the IRA/Plan outright and immediately after the death of one or more prior beneficiaries, then any subsequent beneficiary can be ignored as mere successor beneficiaries.[79] For example, the Accumulation Trust can provide that the Trust will be held for the client's lineal descendants who are then living, provided that if the client has no lineal descendants upon his death, then the trust assets will be paid outright to his last living descendant's issue. Because the trust assets will be distributed outright and immediately to the Plan Participant's grandchildren if his

[79] Choate, *Life and Death Planning for Retirement Benefits* 6.03.07.

children predecease him, then all other successor beneficiaries can be ignored. The above example will only work if the Plan Participant has grandchildren who are then living at the time of his death.

Another method used to deal with this contingent beneficiary issue under an Accumulation Trust is called the "circle trust."[80] Under this method, the Accumulation Trust can provide that the Trust will be held for the lineal descendants of a Plan Participant who are then living, and upon the death of such lineal descendants, the trust assets will be distributed outright to the issue of such lineal descendants, provided that if at any time during such lineal descendants' life they have no then living issue, then the trust shall terminate and all assets shall be distributed outright to the Plan Participant's lineal descendants. This language "closes the circle" of possible successor beneficiaries; so that there are no potential successor beneficiaries that have to be counted in determining the applicable distribution period.

F. Prevent the Adoption or Addition of an Older Beneficiary.

The trust instrument should prevent any individual who is older than a Designated Beneficiary from being considered as a beneficiary of any Accumulation Trust that is the recipient of IRA/Plan benefits from a Plan Participant that died prior to January 1, 2020, or from being considered as a beneficiary of any Accumulation Trust that will be held for the sole lifetime benefit of a disabled or chronically ill beneficiary and will be the recipient of IRA/Plan benefits from a Plan Participant that died on or after January 1, 2020. Further, any such trust agreement should provide that any person to be adopted and qualified to receive benefits would need to be younger than the otherwise applicable Designated Beneficiary under an Accumulation Trust.

As discussed in Chapter 8, this is less of a concern if the Proposed Regulations are finalized in their present form to provide the ability to disregard certain beneficiaries of a See-Through Trust.

G. QTIPPING an Accumulation Trust

What rules apply to determine what portion of any payments from an IRA/Plan to an Accumulation Trust are income for purposes of defining how much has to be paid out to the Surviving Spouse?

With a Conduit Trust, the Surviving Spouse must receive 100% of the distributions so this analysis may not be pertinent. However, under a QTIP Trust that is an Accumulation Trust, the Surviving Spouse only has to receive the "income" as determined under state law and some or all of an IRA/Plan distribution may consist of a return of principal. The analysis that applies is as follows:

[80] Choate, *Life and Death Planning for Retirement Benefits* 6.03.09.

1. The law in each state will vary with reference to what portion of an IRA/Plan distribution will be considered as income for trust income calculation and distribution purposes. For example, the Uniform Principal and Income Act ("UPIA") states that:

   a. To the extent that a payment is characterized as interest, a dividend, or a payment made in lieu of interest or a dividend, a trustee shall allocate the payment to income.

   b. If no part of a payment is characterized as interest, a dividend, or an equivalent payment, and all or part of the payment is required to be made, a trustee shall allocate to income 10 percent of the part that is required to be made during the accounting period and the balance to principal.

2. The IRS has indicated that the UPIA 10% rule "does not satisfy the [marital deduction income] requirements of sections 20.2056(b)-5(f)(1) and 1.643(b)-1, because the amount of the required minimum distribution is not based on the total return of the IRA."[81]

3. The Employee Benefits Committee of the American College of Trust & Estate Counsel (ACTEC) has expressed concern with respect to the 10% rule and recommended amendment and/or elimination of the 10% provision of the UPIA. A majority of states statutes do not satisfy the marital deduction income requirements so until an amendment is made, planners should exercise caution in this area. Some practical solutions to this problem are discussed in the next section.

4. <u>Practical Solutions</u>

   a. One approach that will work is to treat the IRA as a "trust-within-a-trust". Under this approach, income earned under the IRA is treated as income of the trust to the extent distributed. This approach is only possible when the trustee can easily distinguish the IRA's internal income from principal, meaning that the trustee must be able to determine exactly how much the IRA investments earn in income each year. The IRS has approved this approach for marital deduction trusts.

   b. A second approach is to treat the trust as a unitrust. Under this approach, the beneficiary will receive an annual income payment based upon a fixed percentage of the trust assets each year. This will satisfy the marital deduction requirements if (1) it is permitted by state law and (2) the fixed percentage is no less than 3% and no more

[81] Revenue Ruling 2006-26.

than 5%. This approach was approved by the IRS under Revenue Ruling 2006-26.

5. The Florida Principal and Income Act is a good example of a statute that is based upon the Uniform Principal and Income Act, so the discussion below should be of use to both Florida-based advisors and others.

   a. Florida Statute Section 738.602 governs the character of payments from deferred compensation plans, annuities, and retirement plans or accounts. Florida Statute Section 738.602(4) describes the method a trustee should use to allocate income and principal with respect to payments made. The trustee is required to follow the steps set forth below in allocating a payment to principal or income:

      i. If the payor characterized a portion of the payment as income, that portion shall be allocated to income by the trustee and the remaining portion shall be allocated to principal.

      ii. If the payor does not characterize a portion as income, then the following shall apply:

         1. The trustee must attempt to determine the income derived from the applicable investment (i.e. the account statement for a mutual fund). The trustee can then allocate the lesser of the income of the fund, or the entire payment to income, and the remaining portion to principal.

         2. If the trustee "acting reasonably and in good faith" determines that neither A nor B is available, the trustee shall allocate 10% of the payment to income and the remaining portion to principal. Florida's Principal and Income Act requires the trustee to invest trust assets on a "total return basis" and gives the trustee the ability to adjust income so that the treatment of income is "fair and reasonable" to the beneficiary.[82]

   b. Florida law also states that certain unitrusts mandating annual payouts between 3% - 5% will be treated as trusts requiring the payments of all income.[83]

   c. Treas. Reg. § 1.643(b)-1 specifically states that:

[82] Fla. Stat. § 738.103(2), 738.104(1) (2019).
[83] Fla. Stat. § 738.1041(10) (2019).

A state statute providing that income is a unitrust amount of no less than 3% and no more than 5% of the fair market value of the trust assets, whether determined annually or averaged on a multiple year basis, is a reasonable apportionment of the total return of the trust. Similarly, a state statute that permits the trustee to make adjustments between income and principal to fulfill the trustee's duty of impartiality between the income and remainder beneficiaries is generally a reasonable apportionment of the total return of the trust.

d. It is likely that Florida's Uniform Principal and Income Act will satisfy the all-income-for-life requirement of Treas. Reg. § 20.2056(b)-5(f)(1) and Treas. Reg. § 1.643(b)-1 due to the trustee's power to adjust as well as the additional good faith determination requirements for allocating income from a retirement plan.

III. Pre-Secure Act Rules That Apply To Conduit Trusts Only

A. Distributions Must Be Paid to the Trust Beneficiary or Beneficiaries Immediately Following Receipt by the Trustee.

The trustee has no power to accumulate distributions from the IRA/Plan, and any distribution from the IRA/Plan must be paid directly to the trust beneficiaries.[84]

B. Remainder Beneficiaries Do Not Count for Required Minimum Distribution Purposes.

Designated Beneficiaries are treated as sole direct beneficiaries of the IRA/Plan under a Conduit Trust. A Conduit Trust thus can have beneficiaries older than the desired Designated Beneficiary, Non-Persons as beneficiaries, and unlimited power of appointment rights, so long as all distributions from the IRA/Plan to the trust are required to be paid to the Designated Beneficiary upon receipt from the IRA/Plan by trust during his or her lifetime. Remainder beneficiaries are disregarded as mere potential successors and, if older than the Designated Beneficiary, would not cause Required Minimum Distributions to be paid out over a shorter life expectancy or to not be subject to the Life Expectancy or 10-Year Rule, if a Non-Person is a beneficiary as indicated under current Regulations and the 2022 Proposed Regulations.

C. Conduit Trust Can Pay Trust Expenses.

The Designated Beneficiary is treated as the sole beneficiary for Required Minimum Distribution purposes regardless of whether the Conduit Trust can pay

[84] "[A]ll amounts distributed from A's account in Plan X to the trustee while B is alive will be paid directly to B upon receipt by the trustee of Trust P . . . no amounts distributed from A's account in Plan X to Trust P are accumulated in Trust P during B's lifetime for the benefit of any other beneficiary." Treas. Reg. § 1.401(a) (9)-5, A-7(c)(3), Example 2.

expenses. PLR 200432027 and PLR 200432029 concluded that the trust was "a valid, conduit, see-through trust" even though the trust assets could be used to pay expenses.[85]

The following charts illustrate the application of the Required Minimum Distribution rules when the IRA/Plan is payable to a trust if the Plan Participant died prior to January 1, 2020 (the effective date of the SECURE Act). For charts illustrating the application of the Required Minimum Distribution Rules if the Plan Participant died on or after January 1, 2020, see Chapter 7.

[85] PLRs 200432027-200432029 held specifically that the trust was a valid conduit see-through trust and that "The use of Trust T assets to pay expenses associated with the administration of Trust T (in effect, expenses associated with the administration of the Trust T assets for the benefit of Taxpayers B, C, and D) or the possibility, under these facts, that Trust T assets may be required to be used to pay any estate taxes due, in addition to the amount reported on Form 706, does not change this conclusion." This is supported by the proposed regulations that were issued under the SECURE Act on February 24, 2022.

ILLUSTRATION 3.3 – REQUIRED MINIMUM DISTRIBUTIONS

Conduit Trust as Beneficiary (Distributions must be paid to beneficiaries immediately upon receipt from IA or pension by Trustee)

Spouse as Sole Beneficiary

Spouse's distributions need not begin until the later of the year following the Plan Paticipant's death, or the year in which the Plan Participant would have reached age 72 . Treat spouse as the sole individual beneficiary.

Surviving spouse will use the Single Life Table and the RMD Divisor will be recalculated annually.

The Spouse can roll over an IRA/Plan into his or her own plan unless the spouse's withdrawal right is limited by a standard or subject to third-party discretion.

NOTE: RMDs are set at Plan Participant's death and will not change after the death of the Surviving Spouse.

Multiple Beneficiaries

RMDs will begin in the year following the Plan Participant's death.

The RMDs are calculated based upon the life epectancy of the beneficiary who is to receive the required distribution of RMDs from the trust.

NOTE: RMDs are set at Plan Participant's death and will not change after the death of the Surviving Spouse.

Remainder Beneficiaries are disregarded (even if charity, estate, or older Individual).

Sole Individual Conduit Trust

RMDs will bgin in the year following the Plan Participant's death.

The RMDs are calculated based upon the life expectancy of the beneficiary using the Single Life Table, and are NOT recalculated annually.

NOTE: If Plan Particpant has a longer life expectancy than the Designated Beneficiary, then Plan Paticipant's life expectancy can be used to determine RMDs.

Remainder Beneficiaries are disregarded (even if charity, estate, or older individual).

IV. Toggling From A Conduit Trust To An Accumulation Trust (And Vice Versa?)

Private Letter Ruling 200537044 confirmed that it is possible to "Toggle" what would have been a Conduit Trust into an Accumulation Trust on or before the Designation Date (September 30th of the calendar year of death of the Plan Participant). The conversion may only occur once and can be accomplished by providing powers to independent trust protectors named under the trust agreement, if the exercise of such powers will be considered a disclaimer under state law that will result in the disclaimed powers and rights being considered as never having existed (i.e., void ab initio). The trust protectors would have the power to void the provision in the trust agreement that requires that all Required Minimum Distributions be currently distributed to the Designated Beneficiary of the trust. This can enable the trustee to accumulate IRA/Plan distributions in trust and distribute such funds according to his or her discretion.

The Toggle provision described above will typically provide that the following changes will apply when the Toggle switch is flipped:

A. Remove any Non-Person beneficiary as a beneficiary of the trust.

B. Remove any possible individual beneficiary older than the Designated Beneficiary as a possible beneficiary of the trust (if the trust inherited the IRA/Plan upon the Plan Participant's death before January 1, 2020).

C. Restrict any power of appointment over trust assets to be exercisable solely in favor of individuals younger than the Designated Beneficiary (if the trust inherited the IRA/Plan upon the Plan Participant's death before January 1, 2020).

D. A non-generation skipping exempt Conduit Trust, or a Conduit Trust that inherited the IRA/Plan upon the Plan Participant's death before January 1, 2020, need not limit the exercise of any power of appointment to individuals younger than the Designated Beneficiary.

For example, a trust that provides that all IRA/Plan distributions are to be paid to the Surviving Spouse and that a charity is a permissible beneficiary could be changed by having the spouse disclaim the right to receive all IRA/Plan distributions and any power of appointment that he or she has over the IRA/Plan distributions (without disclaiming the right to receive amounts from the trust as needed for health, education, maintenance and support), and the charity can be paid out in full or paid enough so that it agrees to no longer be a beneficiary as of the Designation Date. If the other requirements for an Accumulation Trust are met, then this will be considered to have been successfully toggled to an Accumulation Trust.

Toggling from a Conduit Trust to an Accumulation Trust has several benefits, including creditor protection and asset preservation, especially if the beneficiary is young, unsophisticated, or may have creditor, spendthrift, or divorce risk factors. Several states (including Florida) provide statutory creditor protection for inherited IRA/Plans held by beneficiaries in their individual name, however; any distribution from a retirement plan will not be exempt from the beneficiary's creditors in some states. As further discussed in Chapter 1, Section I (G)(1) of this Handbook, Florida Statute Section 222.21(2)(c) provides that any money or other assets, or any interest in any fund or account that is creditor exempt, does not cease to be exempt by reason of death or a direct transfer or eligible rollover to an inherited IRA/Plan. This is one reason why using an Accumulation Trust will often be favored over leaving an IRA/Plan outright to a Designated Beneficiary or to a Conduit Trust.

Conversely, toggling from an Accumulation Trust to a Conduit Trust could possibly occur by giving Trust Protectors the ability to mandate distribution of all Required Minimum Distributions made to the trust to a specified Designated Beneficiary. This could be beneficial in situations where a beneficiary who previously had creditor issues is free of such issues before September 30th of the year following the year of the death of the Plan Participant. The authors are not aware of any ruling or precedential authority which would permit the toggling of an Accumulation Trust into a Conduit Trust, and the IRS might be less inclined to approve such toggling and may claim that this constitutes the addition of beneficiaries or trust provisions as opposed to a disclaimer or removal.

Caution should be exercised when employing the toggling strategy. The endorsement of this strategy by the IRS has occurred only under the above Private Letter Ruling and the IRS has since indicated that post-death trust modifications will not be favored. The 7th Edition of Natalie Choate's book, *Life and Death Planning for Retirement Benefits*, has the following to say about this:

> ***Some advisors advocate the "switch" trust as a planning technique, seemingly regarding this single rather messy PLR as if it established an IRS-approved prototype trust. Yet the IRS's subsequent turn against post-death trust modifications (see § 4.5.06) makes it unclear whether this PLR could be duplicated today. An alternative view is that the "toggle" approach involves substantial complications, relying on a shaky "precedent," to obtain a modest benefit.***

Natalie's book at Section 4.5.06 states as follows:

> ***"[A]bsent specific authority in the Code or Regulations, the [post-death] modification of [a trust] will not be recognized for federal tax purposes." –Francis V. Sloan, IRS, in PLR 201021038***
>
> ***The post-death "reformation" of the decedent's trust or will should be granted by a court and recognized by the IRS if it appears that (for example) the attorney who drafted the document made a mistake and did not write what the now-deceased client told him to write. But many PLR requests involving post-death reformations do not involve such "scrivener's errors." Rather, it often appears that the income tax effects of the estate plan were simply ignored until after the client's death, at which point "reformation" was used (by collusion among the***

> ***beneficiaries, with the consent of a compliant judge) to redraft the documents in a way that (they hoped) would produce better income tax results. The IRS is not going to accept this type of "reformation." See, e.g., PLR 200944059, in which the participant died leaving his IRA to a trust for the benefit of his Surviving Spouse and issue. The Surviving Spouse and the remainder beneficiaries, with state court blessing, agreed to terminate the trust (so the Surviving Spouse could roll over the IRA held in the trust). The IRS denied the rollover.***

For discussion of "Toggling" on or after January 1, 2020 (the effective date of the SECURE Act), see Chapter 7.

CHAPTER 4 – PAYOUT METHODS THAT APPLY IF THE PLAN PARTICIPANT DIED PRIOR TO JANUARY 1, 2020

The below payout methods generally apply when the Plan Participant has died before January 1, 2020. The SECURE Act and the 2022 Proposed Regulations have made significant changes to the rules that apply when a Plan Participant dies after 2019 and are discussed in detail in Chapters 7 and 8. Readers who are not familiar with this area should review Sections 1, 2, 3, 4 and 5, because these methods of calculation still apply under the SECURE Act.

It is noteworthy that the actual percentage payouts will be different for Plan Participants who die after December 31, 2020 because of new life expectancy assumptions that were released by the Treasury Department.

If an Plan Participant dies before the effective date of the SECURE Act (January 1, 2020), and left a Designated Beneficiary who is receiving distributions over the beneficiary's life expectancy, then the death of the Designated Beneficiary after the effective date of the SECURE Act will cause the 10-Year Rule to apply. For example, the Retirement Plan will have to be distributed in full on or before December 31 of the 10th year following the year of the Designated Beneficiary's death.

The Proposed Regulations clarify that the Designated Beneficiary is treated as an Eligible Designated Beneficiary for the purposes of the ten year payout required under the SECURE Act.

Conversely, if the Designated Beneficiary dies prior to January 1, 2020 then the SECURE Act does not apply with respect to the Retirement Plan held for the benefit of the beneficiaries of such deceased Designated Beneficiary.

The 2022 Proposed Regulations also provide new rules regarding the integration of the SECURE Act provisions where a Plan Participant has died before January 1, 2020, and a trust with multiple beneficiaries receives his or her IRA/Plan following his or her death.

Specifically, the Proposed Regulations provide that if a Plan Participant died before January 1, 2020, and named more than one Designated Beneficiary (such as an Accumulation Trust that has three beneficiaries who are all individuals), then the SECURE Act will apply upon the death of the oldest trust beneficiary, if the trust beneficiary dies on or after January 1, 2020. If the oldest trust beneficiary dies before January 1, 2020 then the SECURE Act does not apply to the trust. In other words, if the

oldest trust beneficiary died before January 1, 2020, then upon such beneficiary's death, payments would continue based upon the life expectancies of the Designated Beneficiaries. If the oldest trust beneficiary died after January 1, 2020, then upon the death of all beneficiaries, the IRA/Plan would need to be distributed within 10 years following the death of the Designated Beneficiary.

See Chapters 7 and 8 for further discussion on the payout rules and other applicable rules established by the SECURE Act and the 2022 Proposed Regulations.

1. Joint Life Expectancy Method ("Uniform Lifetime Table"). See Appendix A, Table A.

   This Table is based upon annual recalculation of the life expectancy of the Plan Participant and a hypothetical spouse who is ten years younger. This Method is used while the Plan Participant is alive, regardless of whether the Plan Participant is married. This Method may also be used by the Surviving Spouse of the original Plan Participant if the Spouse becomes the owner of a spousal rollover IRA/Plan, in which event the Surviving Spouse will be treated as if she is the original Plan Participant. This will not apply if the Spouse treats the Plan of the deceased Plan Participant as an inherited IRA or is the beneficiary of an Accumulation Trust or a Conduit Trust.

   This Method was not changed by the SECURE Act. However, the CARES Act that was enacted on March 27, 2020, modifies the 5-Year Rule to essentially "skip" the year 2020 for the purposes of applying such Rule. Accordingly, the 5-Year Rule becomes a "6-Year Rule" with respect to any situation where (a) a Plan Participant dies between January 1, 2015 and December 31, 2020; and (b) the 5-Year Rule applies. For example, if a Plan Participant died on February 27, 2015, all assets must be distributed from the IRA/Plan no later than December 31, 2021 (instead of by December 31, 2020) as a result of the CARES Act treating the year 2020 as if it did not exist for the purposes of applying the 5-Year Rule.

2. Much Younger Spouse Method ("Joint and Last Survivor Table"). See Appendix A, Table B.

   This Table allows the use of a longer joint life expectancy for annual recalculation during the life of the Plan Participant if both of the following apply:

   a. The spouse of the Plan Participant is more than ten years younger than the Plan Participant; and

   b. The spouse is the *sole* beneficiary of the plan. If the spouse is presently the sole beneficiary of only a portion of a plan, it is best to divide the plan into two separate plans so that he or she can be the sole beneficiary of one plan for this purpose.

A Surviving Spouse who rolls the Plan Participant's Plan into his or her own IRA can use this Method if he or she remarries someone who is more than ten years younger than the Surviving Spouse.

This Method was not changed by the SECURE Act.

3. <u>Recalculated Surviving Spouse One-Life Method ("Single Life Table - Recalculated Annually")</u>. See Appendix A, Table C.

This Method is used for payouts made directly to the Plan Participant's Spouse after the Plan Participant's death where the Spouse is the sole beneficiary of the IRA/Plan that is not rolled over. Additionally, where the Plan Participant's Spouse is the beneficiary of a trust that qualifies as a Conduit Trust, the Spouse's life expectancy can be used and recalculated annually according to the Single Life Table.

The first year distribution is based upon the life expectancy of the Surviving Spouse as listed in the Single Life Table (Table C), which is the Surviving Spouse's oldest age in the *calendar year following* the calendar year of the Plan Participant's death used in determining the Required Minimum Distribution. For each subsequent year, the Applicable Divisor is recalculated based upon the Surviving Spouse's age in each year. For example, if the Surviving Spouse inherits the Plan Participant's IRA/Plan, and she reaches age 72 in the calendar year in which a Required Minimum Distribution must be paid, then the Applicable Divisor will be 15.5. In the following year, when the Surviving Spouse has reached age 73, the Applicable Divisor will be 14.8.

This method was not changed by the SECURE Act.

4. <u>Non-Recalculated One-Life Method – Also Known As "Fixed Term" or "Single Life Reduced by One" Method</u> (Single Life Table is used, with the Applicable Divisor being reduced by one in each year after the first year after the Plan Participant's death). See Appendix A, Table C.

This Method is used where an IRA/Plan is payable as follows:

a. To the Plan Participant's Spouse (after the death of the Plan Participant) where the Plan Participant's Spouse is not the sole primary beneficiary (i.e., the IRA/Plan beneficiary designation or plan document provides that the Spouse and a non-spouse individual or an entity is also named as a primary beneficiary of the applicable IRA/Plan);

b. Directly to, or in a Conduit Trust or Accumulation Trust for, a Non-Spouse Beneficiary after the death of the Plan Participant (if the Plan Participant died before January 1, 2020);

c. Directly to, or in a Conduit Trust for, an Eligible Designated Beneficiary other than the Plan Participant's Surviving Spouse Participant (if the Plan Participant dies on or after January 1, 2020, as discussed in more detail in Chapter 7); or

d. To the beneficiary named by the Plan Participant's Spouse or other non-spouse beneficiary that would inherit the IRA/Plan after the death of the Plan Participant's Spouse or non-spouse beneficiary, as applicable (if the applicable Plan Participant's Spouse or non-spouse beneficiary died before January 1, 2020).

However, this Method will not apply where the Plan Participant's Spouse inherited the Plan Participant's IRA/Plan and rolled it over into his or her own IRA/Plan, subsequently remarried, and left his or her IRA/Plan to his or her new spouse.

The first-year distribution is based upon the life expectancy of the beneficiary as provided in the Single Life Table (Table C). If the Plan Participant's Surviving Spouse is the beneficiary, the Spouse's oldest age in the *calendar year following* the calendar year of the Plan Participant's death is used in determining the Applicable Divisor for calculating the Required Minimum Distributions. If the named beneficiary of the Plan Participant's Spouse is the beneficiary, the beneficiary's oldest age in the *calendar year of* the Spouse's death is used in determining the Required Minimum Distributions.

Each year thereafter, the previous year's Applicable Divisor is reduced by one. Thus, if the first year's Applicable Divisor is 19.5, the second year's Applicable Divisor is 18.5, the third year's Applicable Divisor is 17.5, etc.

If the Plan Participant dies on or after January 1, 2020, this Method is only available if the IRA/Plan is made payable to a minor child (and will apply only until such child reaches age 21), a chronically ill or disabled beneficiary, or a beneficiary not more than ten years younger than the deceased Plan Participant, otherwise the 10-Year Rule will apply, as discussed in more detail in Chapter 7.

5. <u>At-Least-As-Rapidly Rule Method (to Apply Where the Plan Participant Dies After His or Her Required Beginning Date)</u>.

This Method may be used where the Plan Participant dies on or after his or her Required Beginning Date, as discussed in Chapter 2's Crucial Rules.

In such a situation, the IRA/Plan funds must be distributed "at least as rapidly" as they were required to be distributed at the time of the Plan Participant's death; however, the Treasury Regulations provide for a longer distribution period if the Plan Participant has named an individual as Designated Beneficiary, or an Accumulation Trust or a Conduit Trust through which the IRS will look to determine the Designated Beneficiary for Required Minimum Distribution purposes (to the extent that the Life Expectancy Rule applies where an IRA/Plan is left to a Conduit Trust or Accumulation Trust in light of the SECURE Act).

Where a Designated Beneficiary exists, Required Minimum Distributions can be made based upon the Designated Beneficiary's life expectancy (if the life expectancy of the Designated Beneficiary is longer than that of the deceased Plan Participant). Alternatively, the "At-Least-As-Rapidly" Method can be used when the Plan Participant has a longer life expectancy than the Designated Beneficiary in order for a longer distribution period to apply.

Where no Designated Beneficiary exists, Required Minimum Distributions can be made according to the remaining life expectancy of the deceased Plan Participant, notwithstanding whether the beneficiary is an individual, but only if the Plan Participant dies after the Required Beginning Date.

This Method was not changed by the SECURE Act, however, as discussed in more detail in Chapter 7, the "At-Least-As-Rapidly" Method may be beneficial if the deceased Plan Participant died after his or her Required Beginning Date and his or her remaining life expectancy is longer than ten years.

Planning Point for Plan Participant with Terminal Illness - The At-Least-As-Rapidly Rule can work to the advantage of individual plan beneficiaries who are older than a Plan Participant who has a terminal illness if the Plan Participant begins to take distributions to have the Rule apply.

6. Five-Year Rule Method (5th December 31st after the calendar year of death of the Plan Participant- 5th year After Death Payment Requirement, as described above on Page 39).

Under this Method, all account funds must be distributed on or before December 31st of the 5th anniversary of the calendar year of the Plan Participant's death, as described above in Chapter 2's Players and Definitions under the 5-Year Rule. This is the default method if the Plan Participant dies before his or her Required Beginning Date and there is no named Designated Beneficiary, the trust named as a beneficiary does not qualify as an Accumulation Trust or a Conduit Trust, or a non-Person is named as a beneficiary of the IRA/Plan (such as an estate, a charity, a partnership, an LLC, or a corporation).

This Method can be advantageous where the Designated Beneficiary (and the entire realm of potential Designated Beneficiaries) has a life expectancy of under five years, as calculated by the applicable table, or if the Designated Beneficiary has a short life expectancy. It is therefore important to note that the 5-Year Rule is always available to beneficiaries of IRA/Plans, because they can always withdraw more than the Required Minimum Distributions.

This Method was not changed by the SECURE Act.

Below is a summary of the six possible methods for Required Minimum Distributions to be paid out from IRA/Plans and other Qualified Retirement Plans if the Plan Participant died prior to January 1, 2020:

ILLUSTRATION 4.1 –
SIX POSSIBLE METHODS FOR REQUIRED MINIMUM DISTRIBUTIONS

Method 1: "Uniform Life Expectancy Method"	Method 2: "Much Younger Spouse Method"	Method 3: "Recalculated One Life Method"	Method 4: "Non-Recalculated One Life Method"	Method 5: "At-Least-As-Rapidly Method"	Method 6: "5-Year Rule Method"	Alternative Method
WHEN USED:	WHEN USED:	WHEN USED:	WHEN USED:	WHEN USED:	WHEN USED:	WHEN USED:
A. During the lifetime of the Participant, after the Participant attains his or her Required Beginning Date (April 1 of the year after the year in which he or she reaches the age of 70½), unless the Participant's spouse is named as the sole beneficiary of the IRA/Plan and said spouse is more than 10 years younger than the Participant. B. If a Surviving Spouse (i) inherits the Participant's IRA/Plan as the sole beneficiary, and (ii) rolls over	A. During the lifetime of the Participant, once the Participant attains his or her Required Beginning Date, but only if the Participant's spouse is named as the sole beneficiary of the IRA/Plan and said spouse is more than 10 years younger than the Participant. B. If a Surviving Spouse (i) inherits the Participant's IRA/Plan as the sole beneficiary, (ii) rolls over the IRA/Plan into his or her IRA, (iii) subsequently marries a spouse	A. After the death of the Participant, where the Participant's spouse is named as the sole beneficiary of the IRA/Plan (or is the Designated Beneficiary of a Conduit Trust to which the IRA/Plan is payable). 	A. After the death of the Participant, where (i) the Participant's spouse is not named as the sole beneficiary of the IRA/Plan (or is the Designated Beneficiary of an Accumulation Trust to which the IRA/Plan is payable), (ii) a non-spouse individual is named as the beneficiary of the IRA/Plan, or (iii) the Participant's spouse has not rolled over the Participant's IRA/Plan into his or her own IRA, names a beneficiary of the	A. After the death of a Participant who had attained the age of 70½, where (i) no Designated Beneficiary is named with respect to the IRA/Plan, or (ii) the Participant's life expectancy is longer than the Designated Beneficiary's life expectancy. However, if the Participant named a Designated Beneficiary (i.e., an individual or a Trust that qualifies as a Conduit Trust or an Accumulation Trust), and the Designated	A. After the death of a Participant who has not yet attained the age of 70½, where a non-individual (i.e., the Participant's estate, a corporation or other business entity, or a trust that does not qualify as a Conduit Trust or an Accumulation Trust) is named as a beneficiary of the IRA/Plan.	A. If and when the beneficiary would like to receive a life annuity it would be possible to invest the IRA assets with an insurance company in exchange for an annuity contract that will pay a set amount to the beneficiary each year or more frequently for life. This is called an annuitized IRA.

Method 1: "Uniform Life Expectancy Method"	Method 2: "Much Younger Spouse Method"	Method 3: "Recalculated One Life Method"	Method 4: "Non-Recalculated One Life Method"	Method 5: "At-Least-As-Rapidly Method"	Method 6: "5-Year Rule Method"	Alternative Method
the IRA/Plan into his or her IRA.	who is more than 10 years younger than the Surviving Spouse, and (iv) the new spouse is named as the sole beneficiary of Surviving Spouse's IRA.		IRA/Plan, and later dies.	Beneficiary's life expectancy is longer than the Participant's, then this Method is not required to apply and the applicable Method to the left can apply.		
<u>WHICH TABLE TO USE</u>: Uniform Lifetime Table, based on the age of the Participant or Surviving Spouse, as applicable.	<u>WHICH TABLE TO USE</u>: Joint Life and Last Survivor Expectancy Table, based on the ages of the Participant and his or her spouse, or on the ages of the Participant's Surviving Spouse and his or her new spouse.	<u>WHICH TABLE TO USE</u>: Single Life Table, recalculated annually based on the Surviving Spouse's age.	<u>WHICH TABLE TO USE</u>: Single Life Table, based upon the life expectancy of the deceased Participant as if he or she were still living with the applicable divisor reduced by one in each calendar year after the first calendar year following the Participant's death.	<u>WHICH TABLE TO USE</u>: Single Life Table, based upon the life expectancy of the deceased Participant as if he or she were still living, with the applicable divisor reduced by one in each calendar year after the first calendar year following the Participant's death.	<u>WHICH TABLE TO USE</u>: None. All benefits must be distributed from the IRA/Plan by the end of the 5th calendar year after the Participant's death.	<u>WHICH TABLE TO USE</u>: N/A.

IRA rules are extremely complex, and each situation must be analyzed with care. Some scenarios can be tricky, while others are relatively straightforward. Below (Illustration 4.2) are a few examples of those tricky situations that will hopefully assist in avoiding some common errors.

ILLUSTRATION 4.2 - TRICKY PRE-SECURE ACT SITUATIONS

TRICKY SITUATIONS	
Tricky Situation	**Rule**
Plan Participant reaches RBD June 1, 2014. Is the Plan Participant required to take his Required Minimum Distribution in 2014?	No. Plan Participant has the option to take the Required Minimum Distribution prior to the end of 2014 or delay the first year's distribution to April 1st of the following year.
Plan Participant reaches RBD June 1, 2014 but elects to delay his first distribution until April 1, 2015. If Plan Participant dies before taking the distribution, did he die before his Required Beginning Date?	Yes, even if part of the distribution is taken a Plan Participant is determined to have died before his or her Required Beginning Date if he or she dies before April 1 of the year following the death of the Plan Participant.
Beneficiary is 30 when Plan Participant dies on December 31, 2014. Beneficiary turns 31 in June 2015. Is the beneficiary's life expectancy calculated using age 30 or 31?	Age 31. The beneficiary's life expectancy is calculated based upon the age the beneficiary will attain in the calendar year following the Plan Participant's death.
IRA benefits are payable to multiple beneficiaries ages 20, 30, and 50. What age is used to calculate life expectancy?	It Depends. If separate accounts are timely established, life expectancy can be calculated using the age of each individual beneficiary. If separate accounts are not timely established life expectancy is calculated using the age of the oldest beneficiary

See Illustrations 4.3 – 4.6 to determine the Applicable Payment Mode in each beneficiary situation if the Plan Participant died prior to January 1, 2020.

See also WHAT LIFE EXPECTANCY TABLE TO USE AFTER DEATH OF PLAN PARTICIPANT which contains a more detailed description of when each payout method applies.

ILLUSTRATION 4.3 – FOR SURVIVING SPOUSE – PARTICIPANT DIES BEFORE REQUIRED BEGINNING DATE

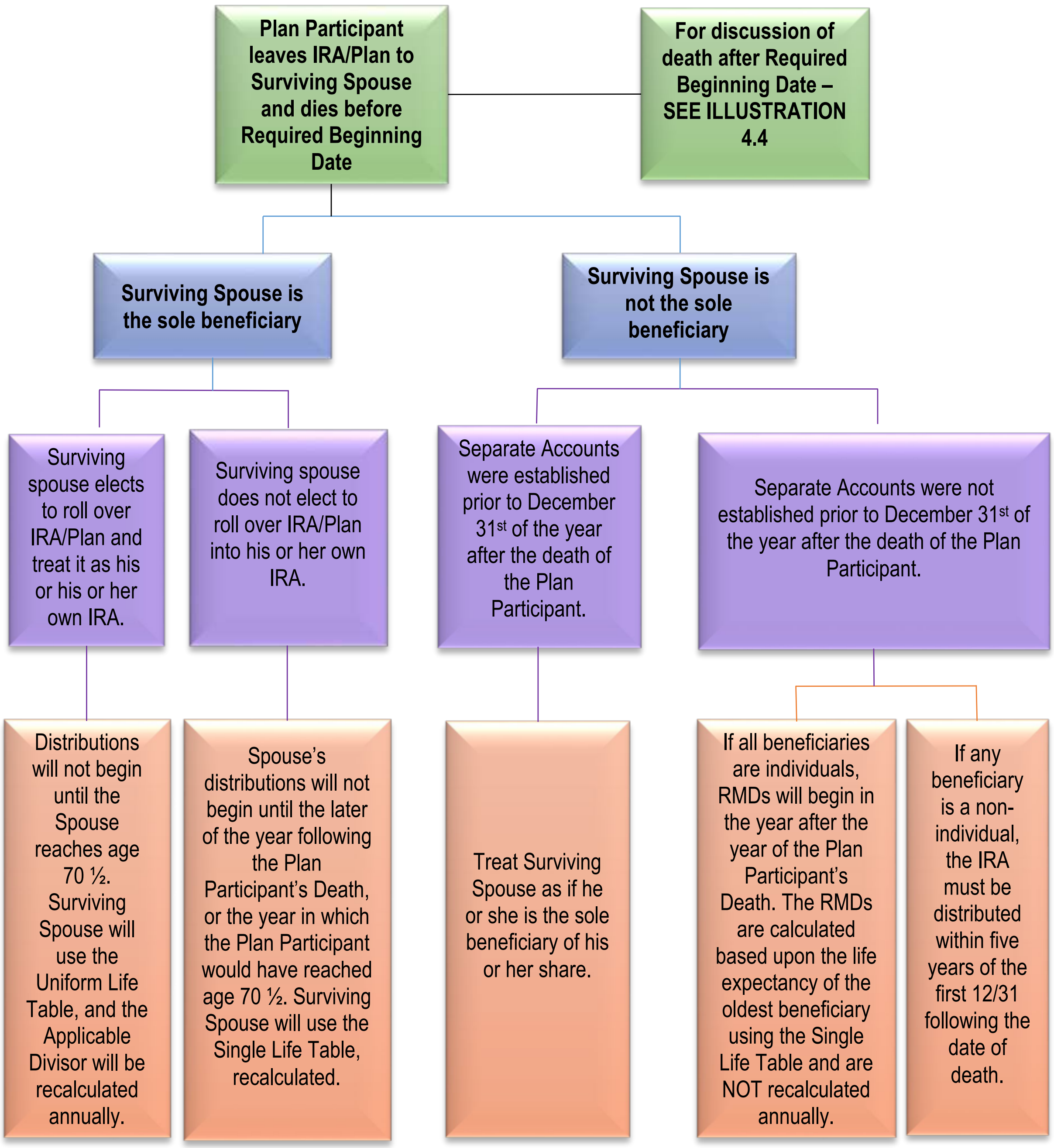


ILLUSTRATION 4.4 – FOR SURVIVING SPOUSE – PARTICIPANT DIES AFTER REQUIRED BEGINNING DATE

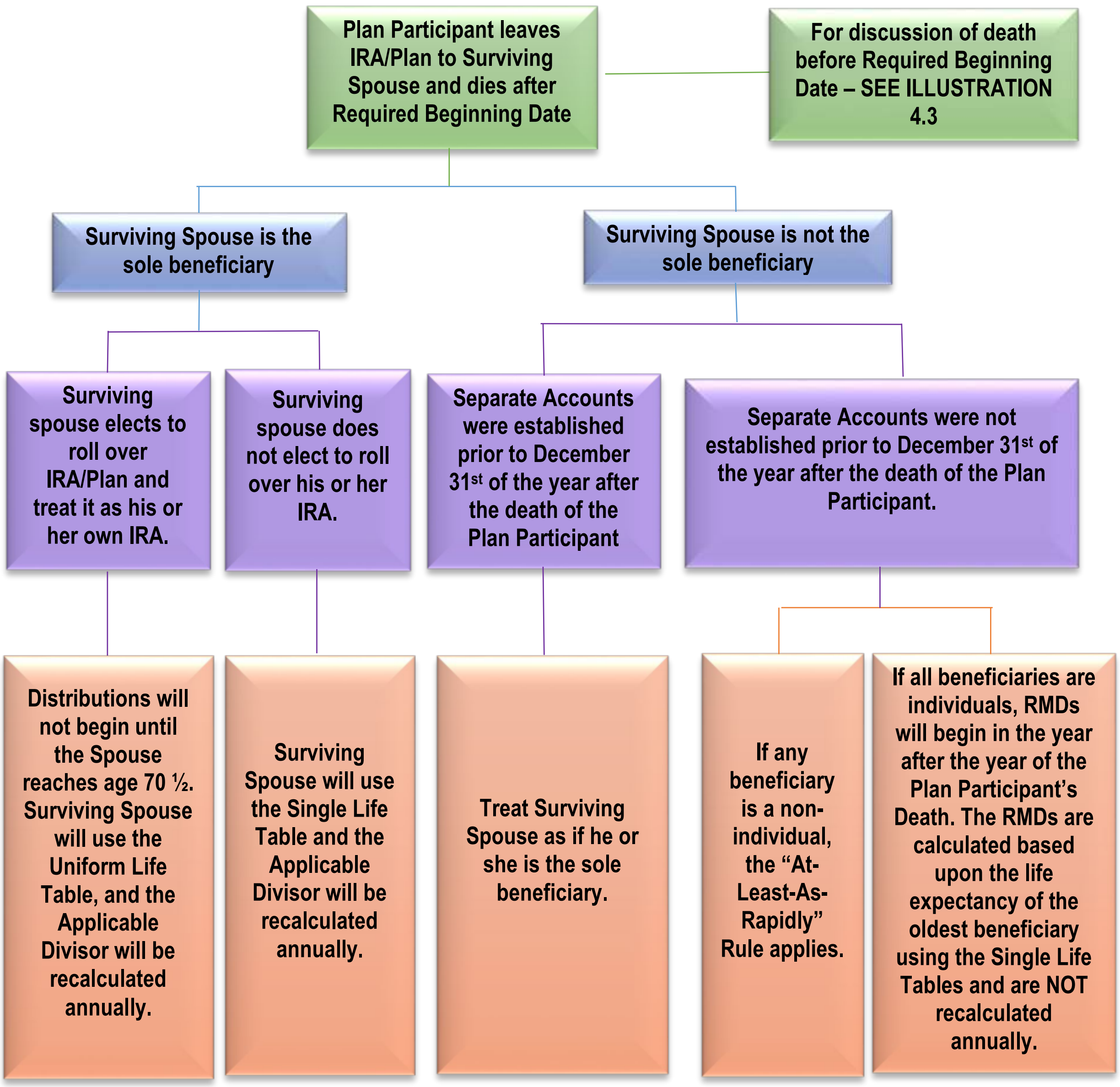


ILLUSTRATION 4.5 – PARTICIPANT DIES LEAVING NO SURVIVING SPOUSE, WITH MULTIPLE BENEFICIARIES BEFORE REQUIRED BEGINNING DATE

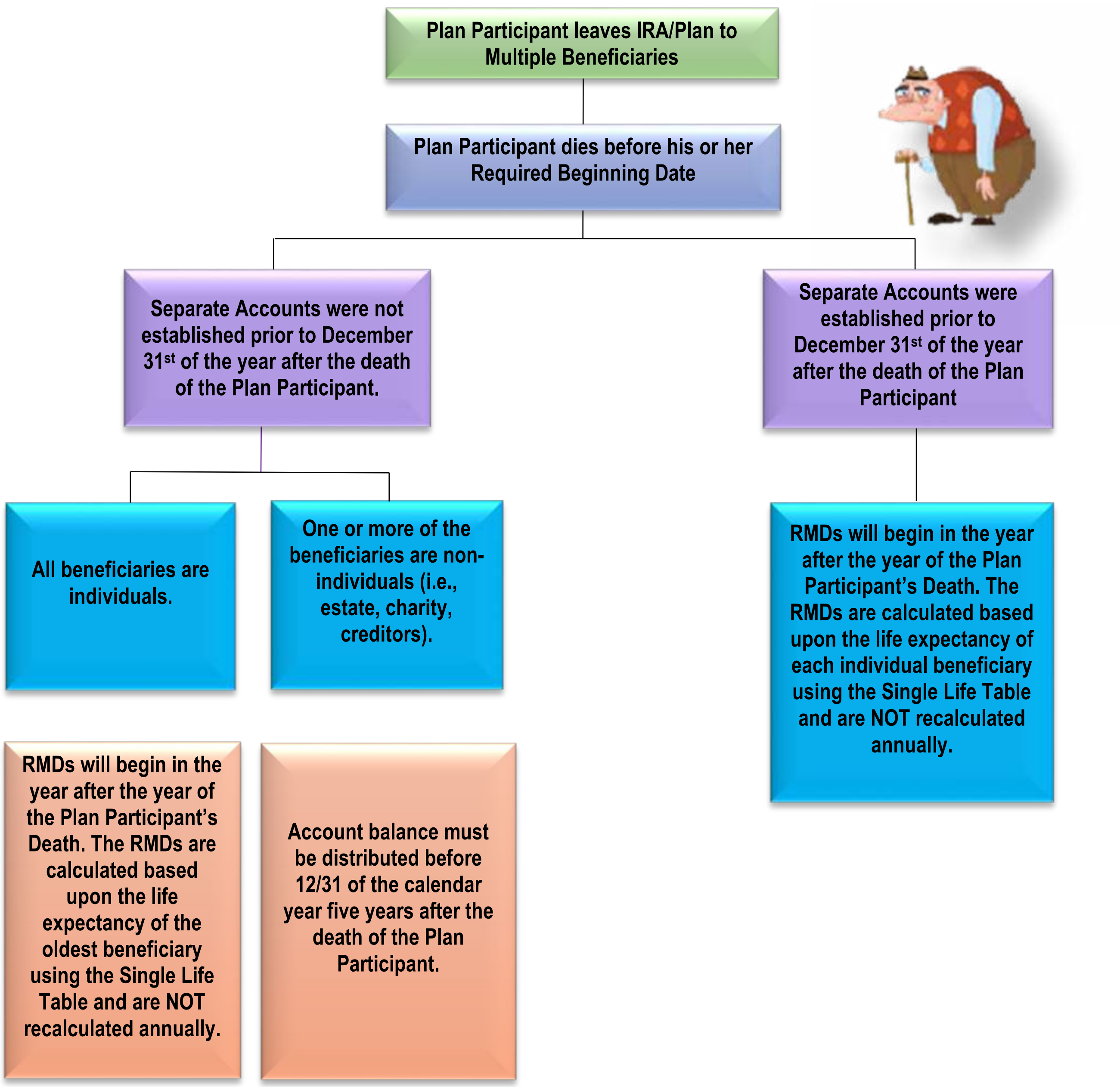


ILLUSTRATION 4.6 –
WHAT LIFE EXPECTANCY TABLE TO USE

What Life Expectancy Table to Use After Death of Plan Participant Before January 1, 2020 (Until the Death of the Designated Beneficiary of the IRA/Plan)

(Differences between Columns 2 and 3 are underlined)

Beneficiary Situation	Plan Participant Dies Before Required Beginning Date	Plan Participant Dies on or After Required Beginning Date
1. Surviving Spouse as sole beneficiary of IRA/Plan (i.e., Surviving Spouse is directly named as beneficiary under the IRA/Plan document or under applicable beneficiary designation, and is not a beneficiary of the IRA/Plan via a trust). This may also apply if the IRA/Plan goes to the estate and the estate goes to the spouse, although it is less certain.	• Surviving Spouse can roll over into his or her own IRA and use Joint Life Expectancy Method based upon Surviving Spouse's age (Uniform Life Table – Table A). If the Surviving Spouse completes the rollover, then distributions need not occur until such Spouse reaches Required Beginning Date • If the Surviving Spouse does not roll over the Plan Participant's account, then the Recalculated One Life Method is used based on the Surviving Spouse's age (Normal Single Life Table – Table C). • If the Surviving Spouse rolls over the Plan Participant's IRA/Plan into his or her own IRA/Plan, then, upon remarriage, the Surviving Spouse may use Much Younger Spouse Method if new spouse is more than ten years younger and is the sole beneficiary of the Surviving Spouse's plan (Joint and Survivor Table – Table B). • If the Surviving Spouse rolls over the Plan Participant's IRA/Plan into his or her own IRA/Plan and subsequently dies before January 1, 2020, naming a new non-spouse Designated Beneficiary, then the new Designated Beneficiary's life expectancy is used based on the Non-Recalculated One Life Method (Single Life Table – Table C in first year, with the Applicable	• Surviving Spouse can roll over into his or her own IRA and use Joint Life Expectancy Method based upon Surviving Spouse's age (Uniform Life Table – Table A). If the Surviving Spouse completes rollover, then distributions need not occur until such Spouse reaches Required Beginning Date. • If the Surviving Spouse does not roll over the Plan Participant's account, then the Recalculated One Life Method is used based on the Surviving Spouse's age (Single Life Table – Table C). • If the Surviving Spouse rolls over the Plan Participant's IRA/Plan into his or her own IRA/Plan, then, upon remarriage, the Surviving Spouse may use Much Younger Spouse Method if new spouse is more than ten years younger and is the sole beneficiary of the Surviving Spouse's plan (Joint and Survivor Table – Table B). • If the Surviving Spouse rolls over the Plan Participant's IRA/Plan into his or her own IRA/Plan and subsequently dies before January 1, 2020, naming a new non-spouse Designated Beneficiary, then the new Designated Beneficiary's life expectancy is used based on the Non-Recalculated One Life Method (Single Life Table—Table C in first year, with the Applicable Divisor reduced by one each year thereafter). • If the Surviving Spouse was older than the Plan Participant, life expectancy can be calculated using

What Life Expectancy Table to Use After Death of Plan Participant Before January 1, 2020 (Until the Death of the Designated Beneficiary of the IRA/Plan) *(Differences between Columns 2 and 3 are underlined)*		
Beneficiary Situation	**Plan Participant Dies Before Required Beginning Date**	**Plan Participant Dies on or After Required Beginning Date**
	Divisor reduced by one each year thereafter). • NOTE – where Surviving Spouse is the sole beneficiary of the Plan Participant's IRA/Plan and the Plan Participant dies before the Required Beginning Date, distributions need not begin until the later of (a) the year after which the Plan Participant dies, or (b) the year when the Plan Participant would have reached age 70½.	the Plan Participant's age, based on the Non-Recalculated One Life Method (Single Life Table – Table C in first year, with the Applicable Divisor reduced by one each year thereafter, in lieu of using the Surviving Spouse's age and the Joint Expectancy Method.
2. Surviving Spouse as beneficiary of Conduit Trust (whereby all Required Minimum Distributions must be paid by Trustee directly to Surviving Spouse.)	• The Recalculated One Life Method is used based on the Surviving Spouse's age (Single Life Table – Table C. • Under a Conduit Trust, the Surviving Spouse is normally not eligible for spousal rollover provisions. A spouse will be eligible for a rollover when the spouse has the right to revoke the trust and withdraw the assets. For situations where a Surviving Spouse was allowed to roll over an IRA, see PLR 9350040, PLR 9416039, PLR 9426049, PLR 200324059 PLR 200634065, PLR 200637033, and PLR 200807025. • NOTE – Where a Conduit Trust for Surviving Spouse is the sole beneficiary of the Plan Participant's IRA/Plan and the Plan Participant dies before the Required Beginning Date, distributions need not begin until the later of (a) the year after which the Plan Participant dies, or (b) the year when the Plan Participant would have reached the Required Beginning Date! If there is any other beneficiary of the Conduit Trust, then distributions must	• The Recalculated One Life Method is used based on the Surviving Spouse's age (Single Life Table – Table C). • Under a Conduit Trust, the Surviving Spouse is normally not eligible for spousal rollover provisions. A spouse will be eligible for a rollover when the spouse has the right to revoke the trust and withdraw the assets. For situations where a Surviving Spouse was allowed to roll over an IRA, see PLR 9350040, PLR 9416039, PLR 9426049, PLR 200324059, PLR 200634065, PLR 200637033, and PLR 200807025. • If the Surviving Spouse was older than the Plan Participant, life expectancy can be calculated using the Plan Participant's age, based on the Non-Recalculated One Life Method (Single Life Table – Table C in first year, with the Applicable Divisor reduced by one each year thereafter), in lieu of using the Surviving Spouse's age and the Joint Expectancy Method. • After the Surviving Spouse's death before January 1, 2020, Required Minimum Distributions must be paid based upon the same Applicable Payment Mode that was in effect

What Life Expectancy Table to Use After Death of Plan Participant Before January 1, 2020 (Until the Death of the Designated Beneficiary of the IRA/Plan)

(Differences between Columns 2 and 3 are underlined)

Beneficiary Situation	Plan Participant Dies Before Required Beginning Date	Plan Participant Dies on or After Required Beginning Date
	begin in the year following the death of the IRA/Plan Participant • NOTE – If Both the Plan Participant and Surviving Spouse as .beneficiary of a Conduit Trust die before the Required Beginning Date, then the IRS has previously ruled that there is no Designated Beneficiary, therefore, subjecting the IRA Distribution to the 5-Year Rule. See PLR 200644022. • After the Surviving Spouse's death before January 1, 2020, Required Minimum Distributions must be paid based upon the same Applicable Payment Mode that was in effect while the Surviving Spouse was alive. Upon the death of the Surviving Spouse on or after January 1, 2020, all assets must be distributed out of the IRA/Plan by December 31 of the 10th year following the calendar year of the Surviving Spouse's death under the 10-Year Rule, even if the Plan Participant died before January 1, 2020.	while the Surviving Spouse was alive. Upon the death of the Surviving Spouse on or after January 1, 2020, all assets must be distributed out of the IRA/Plan by December 31st of the 10th year following the calendar year of the Surviving Spouse's death under the 10-Year Rule, even if the Plan Participant died before January 1, 2020.
3. Surviving Spouse as Designated Beneficiary of Accumulation Trust: (Trust does not require that all IRA/Plan distributions are paid to Surviving Spouse, and the Trustee has the discretion to accumulate or pay out Required Minimum Distributions and other payments from the IRA/Plan).	• The Non-Recalculated One Life Method is used based upon the age of the oldest beneficiary of the Accumulation Trust. (Single Life Table – Table C in first year, with the Applicable Divisor reduced by one each year thereafter). • After the Surviving Spouse's death before January 1, 2020, Required Minimum Distributions must be paid based upon the same Applicable Payment Mode that was in effect while the Surviving Spouse was alive. Upon the death of the Surviving Spouse on or after January 1, 2020,all assets must be distributed out of the IRA/Plan by December 31, of the 10th year	• The Non-Recalculated One Life Method is used based upon the age of the oldest beneficiary of the Accumulation Trust (Single Life Table – Table C in first year, with the Applicable Divisor reduced by one each year thereafter). • After the surviving Spouse's death before January 1, 2020, Required Minimum Distributions must be paid based upon the same Applicable Payment Mode that was in effect while the Surviving Spouse was alive. Upon the death of the Surviving Spouse on or after January 1, 2020, all assets must be distributed out of the IRA/Plan by December 31st of the 10th year following the calendar year

What Life Expectancy Table to Use After Death of Plan Participant Before January 1, 2020 (Until the Death of the Designated Beneficiary of the IRA/Plan)

(Differences between Columns 2 and 3 are underlined)

Beneficiary Situation	Plan Participant Dies Before Required Beginning Date	Plan Participant Dies on or After Required Beginning Date
	following the calendar year of the Surviving Spouse's death under the 10-Year Rule, even if the Plan Participant died before January 1, 2020.	of the Surviving Spouse's death under the 10-Year Rule, even if the Plan Participant died before January 1, 2020.
4. Non-Spouse Beneficiary as the sole direct beneficiary (i.e., such non-spouse beneficiary is directly named as beneficiary under the IRA/Plan document or under the applicable beneficiary designation and is not a beneficiary of the IRA/Plan via a trust).	• The Designated Beneficiary's life expectancy is used based on the Non-Recalculated One Life Method (Single Life Table – Table C in first year, with the Applicable Divisor reduced by one each year thereafter). • After the Designated Beneficiary's death before January 1, 2020, Required Minimum Distributions must be paid based upon the same Applicable Payment Mode that was in effect while the Designated Beneficiary was alive. Upon the death of the Designated Beneficiary on or after January 1, 2020, all assets must be distributed out of the IRA/Plan by December 31st of the 10th year following the calendar year of the Designated Beneficiary's death under the 10-Year Rule, even if the Plan Participant died before January 1, 2020.	• The Designated Beneficiary's life expectancy is used based on the Non-Recalculated One Life Method (Single Life Table – Table C in first year, with the Applicable Divisor reduced by one each year thereafter). • If the beneficiary was older than the Plan Participant, life expectancy can be calculated using the Plan Participant's age, based on the Non-Recalculated One Life Method (Single Life Table – Table C in first year, with the applicable divisor reduced by one each year thereafter), in lieu of using the Surviving Spouse's age and the Joint Expectancy Method. • NOTE: Where a wealthy person wants to benefit low income tax bracket parents, it might be better to leave the IRA/Plan for them than for the children who will be in a higher bracket. • After the Designated Beneficiary's death before January 1, 2020, Required Minimum Distributions must be paid based upon the same Applicable Payment Mode that was in effect while the Designated Beneficiary was alive. Upon the death of the Surviving Spouse on or after January 1, 2020, all assets must be distributed out of the IRA/Plan by December 31st of the 10th year following the calendar year of the Designated Beneficiary's death under the 10-Year Rule, even if the

What Life Expectancy Table to Use After Death of Plan Participant Before January 1, 2020 (Until the Death of the Designated Beneficiary of the IRA/Plan)

(Differences between Columns 2 and 3 are underlined)

Beneficiary Situation	Plan Participant Dies Before Required Beginning Date	Plan Participant Dies on or After Required Beginning Date
		Plan Participant died before January 1, 2020.
5. Non-Spouse as Designated Beneficiary of Conduit Trust (whereby all Required Minimum Distributions must be paid by Trustee directly to such beneficiary).	• The Designated Beneficiary's life expectancy is used based on the Non-Recalculated One Life Method (Single Life Table – Table C in first year, with the Applicable Divisor reduced by one each year thereafter). • After the Designated Beneficiary's death before January 1, 2020, Required Minimum Distributions must be paid based upon the same Applicable Payment Mode that was in effect while the Designated Beneficiary was alive. Upon the death of the Designated Beneficiary on or after January 1, 2020, all assets must be distributed out of the IRA/Plan by December 31st of the 10th year following the calendar year of the Designated Beneficiary's death under the 10-Year Rule, even if the Plan Participant died before January 1, 2020.	• The Designated Beneficiary's life expectancy is used based on the Non-Recalculated One Life Method (Single Life Table – Table C in first year, with the Applicable Divisor reduced by one each year thereafter). • If the beneficiary was older than the Plan Participant, life expectancy can be calculated using the Plan Participant's age, based on the Non-Recalculated One Life Method (Single Life Table – Table C in first year, with the Applicable Divisor reduced by one each year thereafter), in lieu of using the Surviving Spouse's age and the Joint Expectancy Method. • NOTE: Where a wealthy person wants to benefit low income tax bracket parents, it might be better to leave the IRA/Plan for them than for the children who will be in a higher bracket. • After the Designated Beneficiary's death before January 1, 2020, Required Minimum Distributions must be paid based upon the same Applicable Payment Mode that was in effect while the Designated Beneficiary was alive. Upon the death of the Surviving Spouse on or after January 1, 2020, all assets must be distributed out of the IRA/Plan by December 31st of the 10th year following the calendar year of the Designated Beneficiary's death under the 10-Year Rule, even if the Plan Participant died before January 1, 2020.
6. Accumulation Trust with Non-Spouse Designated Beneficiary	• The oldest trust beneficiary's life expectancy is used based on the	

What Life Expectancy Table to Use After Death of Plan Participant Before January 1, 2020 (Until the Death of the Designated Beneficiary of the IRA/Plan) (Differences between Columns 2 and 3 are underlined)		
Beneficiary Situation	**Plan Participant Dies Before Required Beginning Date**	**Plan Participant Dies on or After Required Beginning Date**
(Trust does not require that all IRA/Plan distributions are paid to a particular beneficiary, and the trustee has the discretion to accumulate or pay out Required Minimum Distributions and other payments from the IRA/Plan).	Non-Recalculated One Life Method (Single Life Table – Table C in first year, with the Applicable Divisor reduced by one each year thereafter). • If separate sub-trusts are timely established for multiple Non-Spouse individual beneficiaries, then the life expectancy of each beneficiary of each sub-trust is used based on the Non-Recalculated One Life Method. (Single Life Table – Table C in first year, with the Applicable Divisor reduced by one each year thereafter). • NOTE – Separate accounts established with separate beneficiaries for each account may allow for a separate Required Minimum Distribution calculation for each account. In other words, each beneficiary's life expectancy is used for their separate account instead of the oldest beneficiary's life expectancy being used for all accounts. However, under the Separate Share Rule, an Accumulation Trust must have separate sub-trusts for each beneficiary and the Plan must be payable to the separate sub-trusts in order to have each beneficiary's life expectancy control for that beneficiary's share of the account funds. • After the Designated Beneficiary's death before January 1, 2020, Required Minimum Distributions must be paid based upon the same Applicable Payment Mode that was in effect while the Designated Beneficiary was alive. Upon the death of the Designated Beneficiary on or after January 1,	

What Life Expectancy Table to Use After Death of Plan Participant Before January 1, 2020 (Until the Death of the Designated Beneficiary of the IRA/Plan) (*Differences between Columns 2 and 3 are underlined*)		
Beneficiary Situation	**Plan Participant Dies Before Required Beginning Date**	**Plan Participant Dies on or After Required Beginning Date**
	2020, all assets must be distributed out of the IRA/Plan by December 31st of the 10th year following the calendar year of the Designated Beneficiary's death under the 10-Year Rule, even if the Plan Participant died before January 1, 2020.	

ILLUSTRATION 4.7 – INCOME TAXATION OF AN INHERITED IRA QUICK REFERENCE GUIDE

INCOME TAXATION OF AN INHERITED IRA (INHERITED BEFORE JANUARY 1, 2020) QUICK REFERENCE GUIDE		
I. INDIVIDUAL ORIGINAL PLAN PARTICIPANT OR SURVIVING SPOUSE WHO HAS ROLLED OVER IRA INHERITED FROM PLAN PARTICIPANT	II. SURVIVING SPOUSE AS DESIGNATED BENEFICIARY OF CONDUIT TRUST THAT IS THE BENEFICIARY OF THE IRA/PLAN	III. SPOUSE AS DESIGNATED BENEFICIARY OF AN ACCUMULATION TRUST
A. No withdrawals required until Plan Participant or Surviving Spouse who rolled overreaches the Required Beginning Date.	A. For all purposes, IRA/Plan benefits are deemed as paid to the individual Conduit Trust Designated Beneficiary so Non-Person and older beneficiaries of the trust may exist since they will not directly or indirectly benefit from the IRA/Plan proceeds while the Designated Beneficiary is living.	A. The oldest beneficiary of an Accumulation Trust is the Designated Beneficiary for the purposes of calculating the Required Minimum Distribution. The Surviving Spouse will be the Designated Beneficiary of an Accumulation Trust only if he or she is the oldest beneficiary of the trust.
B. Use Joint Life Expectancy Method (Uniform Lifetime Table-Table A), which is recalculated annually based upon the age of the Plan Participant, or the Surviving Spouse, as applicable	B. If Plan Participant dies before his or her Required Beginning Date, and the Surviving Spouse is the sole beneficiary, then he or she may postpone Required Minimum Distributions until the year that the Plan Participant would have reached the Required Beginning Date.	B. If Plan Participant dies before his or her Required Beginning Date, and the Surviving Spouse is the sole beneficiary, then the Trust may postpone Required Minimum Distributions until the year that the Plan Participant would have reached the Required Beginning Date.

<table>
<tr><th colspan="3">INCOME TAXATION OF AN INHERITED IRA
(INHERITED BEFORE JANUARY 1, 2020)

QUICK REFERENCE GUIDE</th></tr>
<tr>
<td>C. Penalty: 10% excise tax for withdrawals before age 59½ that do not qualify for an exception under Internal Revenue Code Section 72(t)(2), or as a Coronavirus-Related Distribution.</td>
<td>C. If the Plan Participant dies after his or her Required Beginning Date, then distributions can continue to be paid based upon the longer of the remaining life expectancy of the Surviving Spouse, or the remaining life expectancy of the deceased Plan Participant.

DISADVANTAGE – Distributions must be made from the trust to the beneficiary and might be lost to creditors or unwisely spent

NOTE – A Surviving Spouse can only roll over the Plan Participant's IRA/Plan into his or her own, if he or she is the named beneficiary of the plan. In situations where a Conduit Trust is the named beneficiary of the Plan, and the Spouse is the Designated Beneficiary of the Conduit Trust, then the Spouse can only complete a rollover if the Spouse is:

1. The executor of the decedent's estate;

2. Trustee of the trust that is to receive the plan from the decedent; or

3. Otherwise has the unfettered power to require distribution of plan funds. (See PLR 9416039, PLR 9350040, PLR 9426049, PLR 200637033, and PLR 200807025).</td>
<td>C. If the Plan Participant dies after his or her Required Beginning Date, then Required Minimum Distributions can continue to be paid based upon the longer of the remaining life expectancy of the deceased Plan Participant.</td>
</tr>
</table>

INCOME TAXATION OF AN INHERITED IRA (INHERITED BEFORE JANUARY 1, 2020) QUICK REFERENCE GUIDE		
D. On death, the Plan Participant can leave outright to the Surviving Spouse, who can roll the Plan over into his or her own Plan, or leave the IRA/Plan outright or in trust for beneficiaries, who can use their life expectancies for the determination of Required Minimum Distributions, depending on whether the Plan is payable outright or in trust.	D. After the Surviving Spouse's death before January 1, 2020, Required Minimum Distributions must be paid based upon the Spouse's life expectancy, not the younger beneficiaries' life expectancy. Upon the death of the Surviving Spouse on or after January 1, 2020, all assets must be distributed out of the IRA/Plan by December 31st of the 10th year following the calendar year of the Surviving Spouse's death under the 10-Year Rule, even if the Plan Participant died before January 1, 2020.	D. After the Surviving Spouse's death before January 1, 2020, Required Minimum Distributions must be paid based upon the Spouse's life expectancy, not the younger beneficiaries' life expectancy. Upon the death of the Surviving Spouse on or after January 1, 2020, all assets must be distributed out of the IRA/Plan by December 31st of the 10th year following the calendar year of the Surviving Spouse's death under the 10-Year Rule, even if the Plan Participant died before January 1, 2020.
		E. Special Rules apply to QTIP Trust. Specifically, Revenue Ruling 2006-26 outlines the procedure necessary to have a QTIP trust qualify for the estate tax marital deductions as a See-Through Trust. The Revenue Ruling indicates that the QTIP Trust and the IRA/Plan benefit payable to the QTIP Trust must both make an affirmative marital deduction election. Addition- ally, the Surviving Spouse must have the right to require that all income earned within the IRA/Plan is distributed to the QTIP, and then from the QTIP to the Surviving Spouse. Further, the benefits of the IRA/Plan may not be paid out to anyone but the Surviving Spouse during said Spouse's lifetime.
IV. Non-US citizen Surviving Spouse as beneficiary of a QDOT (Qualified Domestic Trust) to qualify IRA for Federal Estate Tax Marital Deduction – Surviving Spouse as Beneficiary of "Grantor Trust" that is the Beneficiary of IRA	**V. Child or other non- spouse individual as Outright Beneficiary**	**VI. Child is Designated Beneficiary of Conduit Trust**

<table>
<tr><th colspan="3">INCOME TAXATION OF AN INHERITED IRA
(INHERITED BEFORE JANUARY 1, 2020)

QUICK REFERENCE GUIDE</th></tr>
<tr><td>A. This arrangement is used primarily when a Surviving Spouse is a resident alien and a QDOT is necessary to obtain the federal estate marital deduction. The Surviving Spouse is treated as the owner of the trust for income tax purposes under Internal Revenue Code Section 678(b) by being given the right to withdraw all trust assets for a given period of time. This is similar to a Conduit Trust because the Spouse is deemed to own the entire trust for income tax purposes if she is given the sole, unrestricted power to withdraw all of the trust assets. The Surviving Spouse is treated as the Designated Beneficiary for Required Minimum Distribution purposes, and she will be responsible for all income tax on the trust's income.</td><td>A. Distributions can be paid out over the life expectancy of the child or other beneficiary. If the beneficiary dies on or after January 1, 2020, then all assets must be distributed out of the IRA/Plan by December 31 of the 10th year following the calendar year of the Designated Beneficiary's death under the 10-Year Rule, even if the Plan Participant died before January 1, 2020.</td><td>The rules are similar to those rules that apply where the Surviving Spouse is the beneficiary of a Conduit Trust (as described in Section II above), with a few notable differences:

A. Required Minimum Distributions must begin by December 31 of the calendar year after the Plan Participant's death, regardless of whether the deceased Plan Participant has reached the Required Beginning Date before death</td></tr>
<tr><td>B. The power to withdraw all trust assets causes the trust to be recognized as a "grantor trust" as to the Surviving Spouse under Subpart E of Subchapter J of the Internal Revenue Code. The deemed "grantor" must be a U.S. resident; it can be an individual other than the Plan Participant's Spouse.</td><td></td><td>B. No one but the Surviving Spouse may roll over the Plan Participant's IRA/Plan into his or her own IRA; thus, the child is unable to complete a rollover; and</td></tr>
<tr><td>C. As with a Conduit Trust, additional beneficiaries can be added to the trust, and regardless of whether they are older or Non-Persons, the Spouse will be considered the Designated Beneficiary because he or she is deemed to be the Designated Beneficiary for the purposes of Required Minimum Distributions.</td><td></td><td>C. There is no marital deduction available for a transfer where a child is the beneficiary of a Conduit Trust.</td></tr>
</table>

INCOME TAXATION OF AN INHERITED IRA (INHERITED BEFORE JANUARY 1, 2020) QUICK REFERENCE GUIDE		
		D. If the child dies on or after January 1, 2020, then all assets must be distributed out of the IRA/Plan by December 31 of the 10th year following the calendar year of the child's death under the 10-Year Rule, even if the Plan Participant died before January 1, 2020 Otherwise, the rules illustrated in Part II are applicable to this situation. **NOTE** – Conduit Trusts are further described below at Section VII. The Designated Beneficiary of the Conduit Trust must have a lifetime right to receive the annual payments, with no trust protectors or third parties having the right to deprive the Designated Beneficiary of this right after the Designation Date. Language for Trust Protector Provision: Notwithstanding the above, the Trust Protector may not remove an individual from having all rights necessary to permit such person from being considered the Designated Beneficiary of any trust that will be subject to the Required Minimum Distribution requirements based upon the life expectancy of such Designated Beneficiary so that the Required Minimum Distribution rules can apply as to any trust that otherwise qualifies as a Conduit Trust or an Accumulation Trust under the Required Minimum Distribution Rules, provided that this shall only apply on or before September 30 of the year after the death of the Plan Participant, and this provision shall not apply with respect to the full satisfaction of the share of a beneficiary under this Trust Agreement.
VII. Child is Designated Beneficiary via an Accumulation Trust	**VIII. Spouse, child, or other individual beneficiary named in a trust that does not qualify as Conduit Trust or Accumulation Trust**	**IX. No separate shares or plans, and a Non-Person Beneficiary**

INCOME TAXATION OF AN INHERITED IRA (INHERITED BEFORE JANUARY 1, 2020) QUICK REFERENCE GUIDE		
The rules are very similar to those rules that apply when the Surviving Spouse is the Designated Beneficiary via an Accumulation Trust, with the following notable differences: A. There is no postponement of the distributions, as Required Minimum Distributions must begin by December 31 of the calendar year after the Plan Participant's death; and	A If a trust does not meet the requirements of either a Conduit Trust or an Accumulation Trust, then there is no Designated Beneficiary for the purposes of the Required Minimum Distribution rules.	A. Only an individual can be a Designated Beneficiary. Non-Persons do not have life expectancies and are therefore not compatible with the tables and tax laws presently drafted.
B. No one but the Surviving Spouse may roll over the Plan Participant's retirement plan into his or her own; therefore, the child is unable to complete a rollover.	B. Consequently, the 5-Year Rule applies, and all account funds must be distributed on or before December 31st of the 5th full calendar year following the date of the Plan Participant's death if the Plan Participant dies before reaching his or her Required Beginning Date; provided that, as a result of the CARES Act, the deadline for distribution of all account funds will be December 31st of the sixth full calendar year if such Plan Participant dies between January 1, 2015 and December 31, 2019. If the Plan Participant dies after reaching his or her Required Beginning Date, then Required Minimum Distributions can be made over the life expectancy of the deceased Plan Participant under the At-Least-As-Rapidly Rule.	B. Therefore, if a Non-Person is a beneficiary of the IRA/ Plan (i.e., an estate, or a trust that does not qualify as a Conduit Trust or an Accumulation Trust), then the 5-Year Rule applies, and all account funds must be distributed on or before the December 31st of the 5th full calendar year following the date of the Plan Participant's death, if the Plan Participant dies before reaching his or her Required Beginning Date; provided that, as a result of the CARES Act, the deadline for distribution of all account funds will be December 31st of the sixth full calendar year if such Plan Participant dies between January 1, 2015 and December 31, 2019. If the Plan Participant dies after reaching his or her Required Beginning Date, then Required Minimum Distributions can be made over the life expectancy of the deceased Plan Participant under the At-Least-As-Rapidly Rule.

INCOME TAXATION OF AN INHERITED IRA (INHERITED BEFORE JANUARY 1, 2020) QUICK REFERENCE GUIDE		
C. Otherwise, the rules illustrated in Part III are applicable to this situation.	C. However, notwithstanding that there is no Designated Beneficiary, if the Plan Participant dies after his or her Required Beginning Date, then distributions can continue to be paid out over the remaining life expectancy of the deceased Plan Participant based on the Non-Recalculated One Life Table Method (Single Life Table-Table C in first year, with the Applicable Required Minimum Distribution Divisor reduced by one each year thereafter).	C. However, notwithstanding that there is no Designated Beneficiary, if the Plan Participant dies after his or her Required Beginning Date, then distributions can continue to be paid out over the remaining life expectancy of the deceased Plan Participant based on the Non Recalculated One Life Method (Single Life Table-Table C in first year, with the Applicable Required Minimum Distribution Divisor reduced by one each year thereafter).
D. If the Plan Participant dies before his or her Required Beginning Date, then no distributions are required until December 31st of the calendar year after the year of the death of the Plan Participant.		D. Where there is a Non-Person beneficiary of a trust that would otherwise qualify as an Accumulation Trust, the removal of such Non-Person beneficiary by the Designation Date (September 30 of the calendar year following the date of the Plan Participant's death) will be sufficient to consider the Non- Person beneficiary to have never existed. Such Non-Person beneficiary may be removed by disclaimer or by satisfaction of the applicable devise or bequest to or for the benefit of such Non-Person beneficiary. The estate of the Plan Participant and/or creditors of the estate of the Plan Participant, including the IRS, would all be considered Non-person beneficiaries for the purposes of the Required Minimum Distribution rules.
E. If the Plan Participant died after his or her Required Beginning Date, then distributions can continue to be paid based upon the longer of the remaining life expectancy of the Designated Beneficiary or the deceased Plan Participant, with the first distribution required to be made by December 31st of the year of the death of the Plan Participant.		

INCOME TAXATION OF AN INHERITED IRA (INHERITED BEFORE JANUARY 1, 2020) QUICK REFERENCE GUIDE		
F. If the child dies on or after January 1, 2020, then all assets must be distributed out of the IRA/Plan by December 31 of the 10th year following the calendar year of the child's death under the 10-Year Rule, even if the Plan Participant died before January 1, 2020.		
X. Where there are no separate shares or plans and separate beneficiaries have separate ages		
A. Unless separate accounts or separate sub-trusts are established for each beneficiary, the oldest beneficiary of an account or Accumulation Trust is the Designated Beneficiary for the purposes of determining Required Minimum Distributions.		
B. The IRS has issued a number of Private Letter Rulings that take the position that a trustee of an Accumulation Trust cannot "after the fact" create separate accounts for the purposes of the Required Minimum Distribution rules. This means that the trust instrument must provide for the initial Accumulation Trust to split into separate sub-trusts for each beneficiary before September 30th in the calendar year following the calendar year of the Plan Participant's death, in order to prevent having the oldest of the trust beneficiaries be the measuring age for the purposes of Required Minimum Distributions. Most trust documents provide for immediate division of trusts for children and will qualify, but oftentimes clients want common assets to be spent for younger children so that their education and upbringing does not cause their inheritance to be less overall than for older siblings. For this situation, it is best to have the separate trusts for each child to receive plan distributions, and to have other assets used to provide such educational and "even up" payments.		
C. If separate distinct sub-trusts are explicitly created under the trust, and the IRA beneficiary designation specifically directs the plan funds to each of those separate sub-trusts, then the age of each beneficiary of each separate sub-trust should control for Required Minimum Distribution purposes. Some commentators believe that it is necessary for the IRA/Plan to be split into separate IRAs during the Plan Participant's life, with each separate IRA naming a different beneficiary, in order for the life expectancy of the applicable named beneficiary to apply with respect to the portion of the IRA/Plan that is payable to his or her respective sub-trust. However, other commentators believe that fractional or percentage dispositions to separate beneficiaries via beneficiary designation will allow the Life Expectancy Rule to apply separately with respect to the portion of the IRA/Plan that is payable to the applicable beneficiary.		

It is important to understand how the different payout methods can affect the longevity of the IRA/Plan after the death of the Plan Participant. For example, when a Surviving Spouse is the sole beneficiary of an IRA/Plan, he or she has the option to either roll over the inherited IRA/Plan into his or her own or elect to be treated as a beneficiary. The election by the Surviving Spouse can have a major effect on the amount and timing of distributions as shown in Illustrations 4.6 through 4.8.[86] Spreadsheets can be created, such as the

[86] The numbers will be updated when the next edition of the book is released, which the authors anticipate to be shortly after the Proposed Regulations are finalized.

ones in Illustrations 4.9 through 4.11 that can analyze the situation and determine the best course of action for the beneficiary. This spreadsheet can also provide clients with an estimate of the dates and amount of the Required Minimum Distributions from the IRA/Plan, as well as an estimate of the account balance based on a hypothetical rate of return.

The set of spreadsheets below analyze a situation in which a 50-year-old Surviving Spouse is deciding whether she will elect to roll over the IRA/Plan into her own. We have assumed that the IRA portfolio will grow at a 6% rate of return. In this situation, it is clear that the Surviving Spouse should roll over the IRA. Based on Illustrations 4.6 and 4.7, if the Surviving Spouse rolls over the IRA, the balance at age 85 will be $4,060,119.45 while the balance if she elects to be treated as a beneficiary will only be $919,674.28, a difference of $3,140,445.17. If the Surviving Spouse can reinvest the Required Minimum Distributions in an investment account in after tax rate of return of 5% the balances of these accounts at age 85 will be $6,480,652,54 for the rolled over IRA and $4,748,483.22 for the non-rolled over IRA.

One alternative to the above is to have the spouse take the IRA as a beneficiary of an Accumulation Trust, in which event, the 10-Year Rule will apply. As illustrated by the third spreadsheet below, this is not as advantageous from a tax standpoint; however, the assets can be held in a much more protected manner. The use of Accumulation Trusts for the Surviving Spouse post-SECURE Act is discussed in more detail in Chapter 7. Below is a detailed spreadsheet for each of the three options, as well as a graph that shows the account balances each year.

50-YEAR OLD SURVIVING SPOUSE AS A BENEFICIARY INHERITED IRA STRETCH REQUIRED MINIMUM DISTRIBUTIONS FOR LIFE, WITH INCOME TAX AT 37%

50 YEAR OLD SURVIVING SPOUSE AS A BENEFICIARY-INHERITED IRA- STRETCH REQUIRED MINIMUM DISTRIBUTIONS FOR LIFE, WITH INCOME TAX AT 37%

A	B	C	D	E	F	G	H	I	J	K	L
Year	Age	Beginning Balance (Value at End of Prior Calendar Year)	Growth at 6%	Required Minimum Distributions Percentage at Applicable Age	Required Minimum Distributions	Income Tax on Required Minimum Distributions (37% Income Tax Rate)	Ending Balance (Value at End of Calendar Year, Assuming That Required Minimum Distributions are Made on Dec. 31)	Investment of Required Minimum Distributions (Column F Minus Column G)	After Tax Growth on Required Minimum Distributions Investment (5%)	Ending Balance of Required Minimum Distributions Investment Account	Total IRA Account and Require Minimum Distributions Investment Account Balance (Column H Plus Column K)
0	50	$1,000,000.00	$60,000.00	2.92%	($29,239.77)	($10,818.71)	$1,030,760.23	$18,421.05	$0.00	$18,421.05	$1,049,181.
1	51	$1,030,760.23	$61,845.61	3.00%	($30,953.76)	($11,452.89)	$1,061,652.09	$19,500.87	$921.05	$38,842.97	$1,100,495.
2	52	$1,061,652.09	$63,699.13	3.10%	($32,868.49)	($12,161.34)	$1,092,482.73	$20,707.15	$1,942.15	$61,492.27	$1,153,975.
3	53	$1,092,482.73	$65,548.96	3.18%	($34,792.44)	($12,873.20)	$1,123,239.25	$21,919.24	$3,074.61	$86,486.12	$1,209,725.
4	54	$1,123,239.25	$67,394.35	3.28%	($36,827.52)	($13,626.18)	$1,153,806.09	$23,201.34	$4,324.31	$114,011.76	$1,267,817.
5	55	$1,153,806.09	$69,228.37	3.38%	($38,979.94)	($14,422.58)	$1,184,054.52	$24,557.36	$5,700.59	$144,269.71	$1,328,324.
6	56	$1,184,054.52	$71,043.27	3.48%	($41,256.25)	($15,264.81)	$1,213,841.53	$25,991.44	$7,213.49	$177,474.64	$1,391,316.
7	57	$1,213,841.53	$72,830.49	3.58%	($43,506.86)	($16,097.54)	$1,243,165.16	$27,409.32	$8,873.73	$213,757.69	$1,456,922.
8	58	$1,243,165.16	$74,589.91	3.70%	($46,043.15)	($17,035.97)	$1,271,711.91	$29,007.19	$10,687.88	$253,452.77	$1,525,164.
9	59	$1,271,711.91	$76,302.71	3.83%	($48,724.59)	($18,028.10)	$1,299,290.03	$30,696.49	$12,672.64	$296,821.90	$1,596,111.
10	60	$1,299,290.03	$77,957.40	3.97%	($51,559.13)	($19,076.88)	$1,325,688.31	$32,482.25	$14,841.09	$344,145.24	$1,669,833.
11	61	$1,325,688.31	$79,541.30	4.10%	($54,331.49)	($20,102.65)	$1,350,898.12	$34,228.84	$17,207.26	$395,581.34	$1,746,479.
12	62	$1,350,898.12	$81,053.89	4.26%	($57,485.03)	($21,269.46)	$1,374,466.98	$36,215.57	$19,779.07	$451,575.98	$1,826,042.
13	63	$1,374,466.98	$82,468.02	4.41%	($60,549.21)	($22,403.21)	$1,396,385.79	$38,146.00	$22,578.80	$512,300.78	$1,908,686.
14	64	$1,396,385.79	$83,783.15	4.59%	($64,054.39)	($23,700.13)	$1,416,114.54	$40,354.27	$25,615.04	$578,270.08	$1,994,384.
15	65	$1,416,114.54	$84,966.87	4.76%	($67,434.03)	($24,950.59)	$1,433,647.39	$42,483.44	$28,913.50	$649,667.02	$2,083,314.
16	66	$1,433,647.39	$86,018.84	4.95%	($70,972.64)	($26,259.88)	$1,448,693.59	$44,712.77	$32,483.35	$726,863.14	$2,175,556.
17	67	$1,448,693.59	$86,921.62	5.15%	($74,674.93)	($27,629.72)	$1,460,940.28	$47,045.20	$36,343.16	$810,251.50	$2,271,191.
18	68	$1,460,940.28	$87,656.42	5.38%	($78,545.18)	($29,061.72)	$1,470,051.52	$49,483.46	$40,512.58	$900,247.54	$2,370,299.
19	69	$1,470,051.52	$88,203.09	5.62%	($82,587.16)	($30,557.25)	$1,475,667.45	$52,029.91	$45,012.38	$997,289.83	$2,472,957.
20	70	$1,475,667.45	$88,540.05	5.88%	($86,803.97)	($32,117.47)	$1,477,403.53	$54,686.50	$49,864.49	$1,101,840.82	$2,579,244.
21	71	$1,477,403.53	$88,644.21	6.13%	($90,638.25)	($33,536.15)	$1,475,409.49	$57,102.10	$55,092.04	$1,214,034.96	$2,689,444.
22	72	$1,475,409.49	$88,524.57	6.45%	($95,187.71)	($35,219.45)	$1,468,746.35	$59,968.26	$60,701.75	$1,334,704.96	$2,803,451.
23	73	$1,468,746.35	$88,124.78	6.76%	($99,239.62)	($36,718.66)	$1,457,631.51	$62,520.96	$66,735.25	$1,463,961.17	$2,921,592.
24	74	$1,457,631.51	$87,457.89	7.09%	($103,378.12)	($38,249.90)	$1,441,711.28	$65,128.22	$73,198.06	$1,602,287.45	$3,043,998.
25	75	$1,441,711.28	$86,502.68	7.46%	($107,590.39)	($39,808.45)	$1,420,623.56	$67,781.95	$80,114.37	$1,750,183.77	$3,170,807.

50-Year Old Surviving Spouse Rolls Over Inherited IRA Into Own Stretch Required Minimum Distributions For Life, with Income Tax at 37%

50 YEAR OLD SURVIVING SPOUSE ROLLS OVER INHERITED IRA INTO OWN IRA- STRETCH REQUIRED MINIMUM DISTRIBUTIONS FOR LIFE, WITH INCOME TAX AT 37%

A	B	C	D	E	F	G	H	I	J	K	L
Year	Age	Beginning Balance (Value at End of Prior Calendar Year)	Growth at 6%	Required Minimum Distributions Percentage at Applicable Age	Required Minimum Distributions	Income Tax on Required Minimum Distributions (37% Income Tax Rate)	Ending Balance (Value at End of Calendar Year, Assuming That Required Minimum Distributions are Made on Dec. 31)	Investment of Required Minimum Distributions (Column F Minus Column G)	After Tax Growth on Required Minimum Distributions Investment (5%)	Ending Balance of Required Minimum Distributions Investment Account	Total IRA Account and Required Minimum Distributions Investment Account Balance (Column K Plus Column H)
26	76	$3,880,588.69	$232,835.32	4.55%	($176,390.40)	($65,264.45)	$3,937,033.62	$111,125.95	$20,770.32	$547,302.72	$4,484,336.34
27	77	$3,937,033.62	$236,222.02	4.72%	($185,709.13)	($68,712.38)	$3,987,546.50	$116,996.75	$27,365.14	$691,664.61	$4,679,211.11
28	78	$3,987,546.50	$239,252.79	4.93%	($196,430.86)	($72,679.42)	$4,030,368.43	$123,751.44	$34,583.23	$849,999.28	$4,880,367.71
29	79	$4,030,368.43	$241,822.11	5.13%	($206,685.56)	($76,473.66)	$4,065,504.98	$130,211.90	$42,499.96	$1,022,711.15	$5,088,216.12
30	80	$4,065,504.98	$243,930.30	5.35%	($217,406.68)	($80,440.47)	$4,092,028.59	$136,966.21	$51,135.56	$1,210,812.92	$5,302,841.51
31	81	$4,092,028.59	$245,521.72	5.59%	($228,604.95)	($84,583.83)	$4,108,945.36	$144,021.12	$60,540.65	$1,415,374.68	$5,524,320.04
32	82	$4,108,945.36	$246,536.72	5.85%	($240,289.20)	($88,907.00)	$4,115,192.88	$151,382.20	$70,768.73	$1,637,525.61	$5,752,718.49
33	83	$4,115,192.88	$246,911.57	6.13%	($252,465.82)	($93,412.35)	$4,109,638.63	$159,053.47	$81,876.28	$1,878,455.36	$5,988,093.99
34	84	$4,109,638.63	$246,578.32	6.45%	($265,137.98)	($98,101.05)	$4,091,078.97	$167,036.92	$93,922.77	$2,139,415.05	$6,230,494.02
35	85	$4,091,078.97	$245,464.74	6.76%	($276,424.25)	($102,276.97)	$4,060,119.45	$174,147.28	$106,970.75	$2,420,533.08	$6,480,652.54
36	86	$4,060,119.45	$243,607.17	7.09%	($287,951.73)	($106,542.14)	$4,015,774.89	$181,409.59	$121,026.65	$2,722,969.33	$6,738,744.22
37	87	$4,015,774.89	$240,946.49	7.46%	($299,684.69)	($110,883.34)	$3,957,036.69	$188,801.36	$136,148.47	$3,047,919.15	$7,004,955.84
38	88	$3,957,036.69	$237,422.20	7.87%	($311,577.69)	($115,283.75)	$3,882,881.20	$196,293.95	$152,395.96	$3,396,609.06	$7,279,490.26
39	89	$3,882,881.20	$232,972.87	8.33%	($323,573.43)	($119,722.17)	$3,792,280.64	$203,851.26	$169,830.45	$3,770,290.77	$7,562,571.41
40	90	$3,792,280.64	$227,536.84	8.77%	($332,656.20)	($123,082.79)	$3,687,161.28	$209,573.40	$188,514.54	$4,168,378.72	$7,855,539.99
41	91	$3,687,161.28	$221,229.68	9.26%	($341,403.82)	($126,319.41)	$3,566,987.13	$215,084.41	$208,418.94	$4,591,882.06	$8,158,869.19
42	92	$3,566,987.13	$214,019.23	9.80%	($349,704.62)	($129,390.71)	$3,431,301.74	$220,313.91	$229,594.10	$5,041,790.07	$8,473,091.81
43	93	$3,431,301.74	$205,878.10	10.42%	($357,427.26)	($132,248.09)	$3,279,752.58	$225,179.18	$252,089.50	$5,519,058.75	$8,798,811.33
44	94	$3,279,752.58	$196,785.15	10.99%	($360,412.37)	($133,352.58)	$3,116,125.36	$227,059.79	$275,952.94	$6,022,071.49	$9,138,196.85
45	95	$3,116,125.36	$186,967.52	11.63%	($362,340.16)	($134,065.86)	$2,940,752.73	$228,274.30	$301,103.57	$6,551,449.36	$9,492,202.09
46	96	$2,940,752.73	$176,445.16	12.35%	($363,055.89)	($134,330.68)	$2,754,142.00	$228,725.21	$327,572.47	$7,107,747.04	$9,861,889.04
47	97	$2,754,142.00	$165,248.52	13.16%	($362,387.10)	($134,083.23)	$2,557,003.41	$228,303.88	$355,387.35	$7,691,438.27	$10,248,441.68
48	98	$2,557,003.41	$153,420.20	14.08%	($360,141.33)	($133,252.29)	$2,350,282.29	$226,889.04	$384,571.91	$8,302,899.22	$10,653,181.51
49	99	$2,350,282.29	$141,016.94	14.93%	($350,788.40)	($129,791.71)	$2,140,510.83	$220,996.69	$415,144.96	$8,939,040.87	$11,079,551.70
50	100	$2,140,510.83	$128,430.65	15.87%	($339,763.62)	($125,712.54)	$1,929,177.85	$214,051.08	$446,952.04	$9,600,044.00	$11,529,221.85

50-Year Old Surviving Spouse as a Beneficiary Inherited IRA Stretch Required Minimum Distributions For Life, with Income Tax at 37%

50 YEAR OLD SURVIVING SPOUSE AS A BENEFICIARY-INHERITED IRA- STRETCH REQUIRED MINIMUM DISTRIBUTIONS FOR LIFE, WITH INCOME TAX AT 37%

A	B	C	D	E	F	G	H	I	J	K	L
Year	Age	Beginning Balance (Value at End of Prior Calendar Year)	Growth at 6%	Required Minimum Distributions Percentage at Applicable Age	Required Minimum Distributions	Income Tax on Required Minimum Distributions (37% Income Tax Rate)	Ending Balance (Value at End of Calendar Year, Assuming That Required Minimum Distributions are Made on Dec. 31)	Investment of Required Minimum Distributions (Column F Minus Column G)	After Tax Growth on Required Minimum Distributions Investment (5%)	Ending Balance of Required Minimum Distributions Investment Account	Total IRA Account and Required Minimum Distributions Investment Account Balance (Column H Plus Column K)
0	50	$1,000,000.00	$60,000.00	2.92%	($29,239.77)	($10,818.71)	$1,030,760.23	$18,421.05	$0.00	$18,421.05	$1,049,181.29
1	51	$1,030,760.23	$61,845.61	3.00%	($30,953.76)	($11,452.89)	$1,061,652.09	$19,500.87	$921.05	$38,842.97	$1,100,495.06
2	52	$1,061,652.09	$63,699.13	3.10%	($32,868.49)	($12,161.34)	$1,092,482.73	$20,707.15	$1,942.15	$61,492.27	$1,153,975.00
3	53	$1,092,482.73	$65,548.96	3.18%	($34,792.44)	($12,873.20)	$1,123,239.25	$21,919.24	$3,074.61	$86,486.12	$1,209,725.37
4	54	$1,123,239.25	$67,394.35	3.28%	($36,827.52)	($13,626.18)	$1,153,806.09	$23,201.34	$4,324.31	$114,011.76	$1,267,817.85
5	55	$1,153,806.09	$69,228.37	3.38%	($38,979.94)	($14,422.58)	$1,184,054.52	$24,557.36	$5,700.59	$144,269.71	$1,328,324.23
6	56	$1,184,054.52	$71,043.27	3.48%	($41,256.25)	($15,264.81)	$1,213,841.53	$25,991.44	$7,213.49	$177,474.64	$1,391,316.17
7	57	$1,213,841.53	$72,830.49	3.58%	($43,506.86)	($16,097.54)	$1,243,165.16	$27,409.32	$8,873.73	$213,757.69	$1,456,922.85
8	58	$1,243,165.16	$74,589.91	3.70%	($46,043.15)	($17,035.97)	$1,271,711.91	$29,007.19	$10,687.88	$253,452.77	$1,525,164.68
9	59	$1,271,711.91	$76,302.71	3.83%	($48,724.59)	($18,028.10)	$1,299,290.03	$30,696.49	$12,672.64	$296,821.90	$1,596,111.93
10	60	$1,299,290.03	$77,957.40	3.97%	($51,559.13)	($19,076.88)	$1,325,688.31	$32,482.25	$14,841.09	$344,145.24	$1,669,833.55
11	61	$1,325,688.31	$79,541.30	4.10%	($54,331.49)	($20,102.65)	$1,350,898.12	$34,228.84	$17,207.26	$395,581.34	$1,746,479.46
12	62	$1,350,898.12	$81,053.89	4.26%	($57,485.03)	($21,269.46)	$1,374,466.98	$36,215.57	$19,779.07	$451,575.98	$1,826,042.96
13	63	$1,374,466.98	$82,468.02	4.41%	($60,549.21)	($22,403.21)	$1,396,385.79	$38,146.00	$22,578.80	$512,300.78	$1,908,686.57
14	64	$1,396,385.79	$83,783.15	4.59%	($64,054.39)	($23,700.13)	$1,416,114.54	$40,354.27	$25,615.04	$578,270.08	$1,994,384.63
15	65	$1,416,114.54	$84,966.87	4.76%	($67,434.03)	($24,950.59)	$1,433,647.39	$42,483.44	$28,913.50	$649,667.02	$2,083,314.42
16	66	$1,433,647.39	$86,018.84	4.95%	($70,972.64)	($26,259.88)	$1,448,693.59	$44,712.77	$32,483.35	$726,863.14	$2,175,556.73
17	67	$1,448,693.59	$86,921.62	5.15%	($74,674.93)	($27,629.72)	$1,460,940.28	$47,045.20	$36,343.16	$810,251.50	$2,271,191.78
18	68	$1,460,940.28	$87,656.42	5.38%	($78,545.18)	($29,061.72)	$1,470,051.52	$49,483.46	$40,512.58	$900,247.54	$2,370,299.06
19	69	$1,470,051.52	$88,203.09	5.62%	($82,587.16)	($30,557.25)	$1,475,667.45	$52,029.91	$45,012.38	$997,289.83	$2,472,957.28
20	70	$1,475,667.45	$88,540.05	5.88%	($86,803.97)	($32,117.47)	$1,477,403.53	$54,686.50	$49,864.49	$1,101,840.82	$2,579,244.35
21	71	$1,477,403.53	$88,644.21	6.13%	($90,638.25)	($33,536.15)	$1,475,409.49	$57,102.10	$55,092.04	$1,214,034.96	$2,689,444.44
22	72	$1,475,409.49	$88,524.57	6.45%	($95,187.71)	($35,219.45)	$1,468,746.35	$59,968.26	$60,701.75	$1,334,704.96	$2,803,451.31
23	73	$1,468,746.35	$88,124.78	6.76%	($99,239.62)	($36,718.66)	$1,457,631.51	$62,520.96	$66,735.25	$1,463,961.17	$2,921,592.68
24	74	$1,457,631.51	$87,457.89	7.09%	($103,378.12)	($38,249.90)	$1,441,711.28	$65,128.22	$73,198.06	$1,602,287.45	$3,043,998.72
25	75	$1,441,711.28	$86,502.68	7.46%	($107,590.39)	($39,808.45)	$1,420,623.56	$67,781.95	$80,114.37	$1,750,183.77	$3,170,807.33

50-YEAR OLD SURVIVING SPOUSE AS A BENEFICIARY INHERITED IRA STRETCH REQUIRED MINIMUM DISTRIBUTIONS FOR LIFE, WITH INCOME TAX AT 37%

50 YEAR OLD SURVIVING SPOUSE AS A BENEFICIARY-INHERITED IRA- STRETCH REQUIRED MINIMUM DISTRIBUTIONS FOR LIFE, WITH INCOME TAX AT 37%

A	B	C	D	E	F	G	H	I	J	K	L
Year	Age	Beginning Balance (Value at End of Prior Calendar Year)	Growth at 6%	Required Minimum Distributions Percentage at Applicable Age	Required Minimum Distributions	Income Tax on Required Minimum Distributions (37% Income Tax Rate)	Ending Balance (Value at End of Calendar Year, Assuming That Required Minimum Distributions are Made on Dec. 31)	Investment of Required Minimum Distributions (Column F Minus Column G)	After Tax Growth on Required Minimum Distributions Investment (5%)	Ending Balance of Required Minimum Distributions Investment Account	Total IRA Account and R Minimum Distributi Investment Account B (Column H Plus Colur
26	76	$1,420,623.56	$85,237.41	7.87%	($111,860.12)	($41,388.25)	$1,394,000.85	$70,471.88	$87,509.19	$1,908,164.83	$3,30
27	77	$1,394,000.85	$83,640.05	8.26%	($115,206.68)	($42,626.47)	$1,362,434.22	$72,580.21	$95,408.24	$2,076,153.28	$3,43
28	78	$1,362,434.22	$81,746.05	8.77%	($119,511.77)	($44,219.36)	$1,324,668.50	$75,292.42	$103,807.66	$2,255,253.37	$3,57
29	79	$1,324,668.50	$79,480.11	9.26%	($122,654.49)	($45,382.16)	$1,281,494.12	$77,272.33	$112,762.67	$2,445,288.36	$3,72
30	80	$1,281,494.12	$76,889.65	9.80%	($125,636.68)	($46,485.57)	$1,232,747.09	$79,151.11	$122,264.42	$2,646,703.89	$3,87
31	81	$1,232,747.09	$73,964.83	10.31%	($127,087.33)	($47,022.31)	$1,179,624.58	$80,065.02	$132,335.19	$2,859,104.10	$4,03
32	82	$1,179,624.58	$70,777.48	10.99%	($129,629.08)	($47,962.76)	$1,120,772.98	$81,666.32	$142,955.20	$3,083,725.62	$4,20
33	83	$1,120,772.98	$67,246.38	11.63%	($130,322.44)	($48,219.30)	$1,057,696.92	$82,103.14	$154,186.28	$3,320,015.04	$4,37
34	84	$1,057,696.92	$63,461.82	12.35%	($130,579.87)	($48,314.55)	$990,578.87	$82,265.32	$166,000.75	$3,568,281.11	$4,55
35	85	$990,578.87	$59,434.73	13.16%	($130,339.33)	($48,225.55)	$919,674.28	$82,113.77	$178,414.06	$3,828,808.94	$4,74
36	86	$919,674.28	$55,180.46	14.08%	($129,531.59)	($47,926.69)	$845,323.15	$81,604.90	$191,440.45	$4,101,854.29	$4,94
37	87	$845,323.15	$50,719.39	14.93%	($126,167.63)	($46,682.02)	$769,874.90	$79,485.61	$205,092.71	$4,386,432.61	$5,15
38	88	$769,874.90	$46,192.49	15.87%	($122,202.37)	($45,214.88)	$693,865.03	$76,987.49	$219,321.63	$4,682,741.73	$5,37
39	89	$693,865.03	$41,631.90	16.95%	($117,604.24)	($43,513.57)	$617,892.69	$74,090.67	$234,137.09	$4,990,969.49	$5,60
40	90	$617,892.69	$37,073.56	18.18%	($112,344.13)	($41,567.33)	$542,622.13	$70,776.80	$249,548.47	$5,311,294.76	$5,85
41	91	$542,622.13	$32,557.33	19.23%	($104,350.41)	($38,609.65)	$470,829.04	$65,740.76	$265,564.74	$5,642,600.26	$6,11
42	92	$470,829.04	$28,249.74	20.41%	($96,087.56)	($35,552.40)	$402,991.23	$60,535.16	$282,130.01	$5,985,265.44	$6,38
43	93	$402,991.23	$24,179.47	21.74%	($87,606.79)	($32,414.51)	$339,563.91	$55,192.28	$299,263.27	$6,339,720.98	$6,67
44	94	$339,563.91	$20,373.83	23.26%	($78,968.35)	($29,218.29)	$280,969.40	$49,750.06	$316,986.05	$6,706,457.10	$6,98
45	95	$280,969.40	$16,858.16	24.39%	($68,529.12)	($25,355.77)	$229,298.44	$43,173.35	$335,322.85	$7,084,953.30	$7,31
46	96	$229,298.44	$13,757.91	26.32%	($60,341.69)	($22,326.43)	$182,714.65	$38,015.27	$354,247.66	$7,477,216.23	$7,65
47	97	$182,714.65	$10,962.88	27.78%	($50,754.07)	($18,779.01)	$142,923.46	$31,975.06	$373,860.81	$7,883,052.10	$8,02
48	98	$142,923.46	$8,575.41	29.41%	($42,036.31)	($15,553.44)	$109,462.56	$26,482.88	$394,152.61	$8,303,687.59	$8,41
49	99	$109,462.56	$6,567.75	32.26%	($35,310.50)	($13,064.89)	$80,719.81	$22,245.62	$415,184.38	$8,741,117.58	$8,82
50	100	$80,719.81	$4,843.19	34.48%	($27,834.42)	($10,298.73)	$57,728.58	$17,535.68	$437,055.88	$9,195,709.14	$9,25

50-YEAR OLD NON-SPOUSE BENEFICIARY OF INHERITED IRA FULL WITHDRAWAL OF IRA REQUIRED WITHIN 10 YEARS

50 YEAR OLD NON-SPOUSE BENEFICIARY OF INHERITED IRA- FULL WITHDRAWAL OF IRA REQUIRED WITHIN 10 YEARS

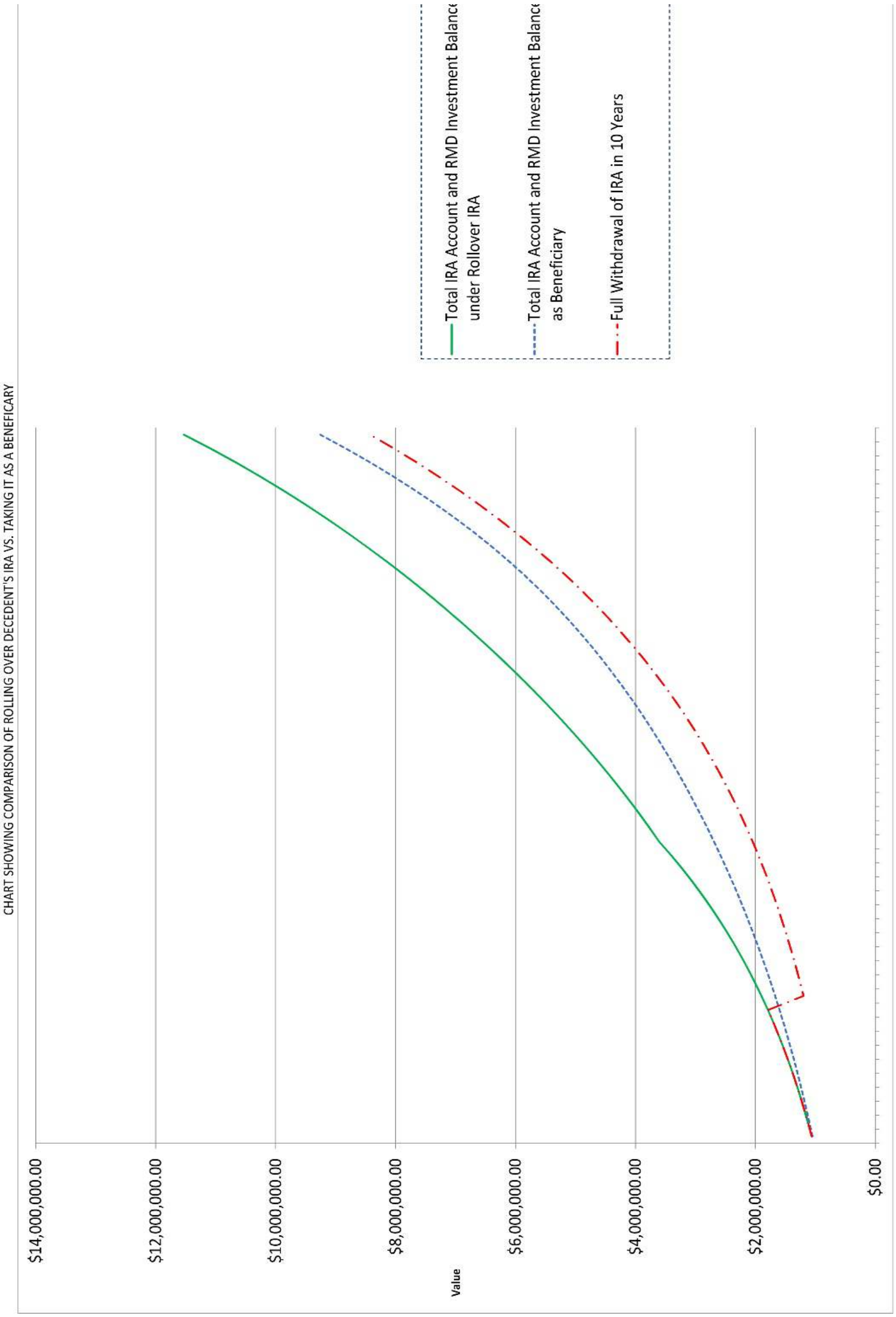
A	B	C	D	E	F	G	H	I	J	K
Year	Age	Beginning Balance (Value at End of Prior Calendar Year)	Growth at 6%	Complete Distribution at Age 60	Income Tax on Distributions (37% Income Tax Rate)	Ending Balance (Value at End of Calendar Year, Assuming That Distribution is Made on Dec. 31)	Investment of Distributions (Column F Minus Column G)	After Tax Growth on Distributions Investment (5%)	Ending Balance of Distribution Investment Account	Total IRA Account and Required Minimum Distributions Investment Account Balance (Column G Plus Column J)
0	50	$1,000,000.00	$60,000.00	$0.00	$0.00	$1,060,000.00	$0.00	$0.00	$0.00	$1,060,000.00
1	51	$1,060,000.00	$63,600.00	$0.00	$0.00	$1,123,600.00	$0.00	$0.00	$0.00	$1,123,600.00
2	52	$1,123,600.00	$67,416.00	$0.00	$0.00	$1,191,016.00	$0.00	$0.00	$0.00	$1,191,016.00
3	53	$1,191,016.00	$71,460.96	$0.00	$0.00	$1,262,476.96	$0.00	$0.00	$0.00	$1,262,476.96
4	54	$1,262,476.96	$75,748.62	$0.00	$0.00	$1,338,225.58	$0.00	$0.00	$0.00	$1,338,225.58
5	55	$1,338,225.58	$80,293.53	$0.00	$0.00	$1,418,519.11	$0.00	$0.00	$0.00	$1,418,519.11
6	56	$1,418,519.11	$85,111.15	$0.00	$0.00	$1,503,630.26	$0.00	$0.00	$0.00	$1,503,630.26
7	57	$1,503,630.26	$90,217.82	$0.00	$0.00	$1,593,848.07	$0.00	$0.00	$0.00	$1,593,848.07
8	58	$1,593,848.07	$95,630.88	$0.00	$0.00	$1,689,478.96	$0.00	$0.00	$0.00	$1,689,478.96
9	59	$1,689,478.96	$101,368.74	$0.00	$0.00	$1,790,847.70	$0.00	$0.00	$0.00	$1,790,847.70
10	60	$1,790,847.70	$107,450.86	($1,898,298.56)	($702,370.47)	$0.00	$1,195,928.09	$0.00	$1,195,928.09	$1,195,928.09
11	61	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$59,796.40	$1,255,724.50	$1,255,724.50
12	62	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$62,786.22	$1,318,510.72	$1,318,510.72
13	63	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$65,925.54	$1,384,436.26	$1,384,436.26
14	64	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$69,221.81	$1,453,658.07	$1,453,658.07
15	65	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$72,682.90	$1,526,340.97	$1,526,340.97
16	66	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$76,317.05	$1,602,658.02	$1,602,658.02
17	67	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$80,132.90	$1,682,790.92	$1,682,790.92
18	68	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$84,139.55	$1,766,930.47	$1,766,930.47
19	69	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$88,346.52	$1,855,276.99	$1,855,276.99
20	70	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$92,763.85	$1,948,040.84	$1,948,040.84
21	71	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$97,402.04	$2,045,442.88	$2,045,442.88
22	72	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$102,272.14	$2,147,715.03	$2,147,715.03
23	73	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$107,385.75	$2,255,100.78	$2,255,100.78
24	74	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$112,755.04	$2,367,855.82	$2,367,855.82
25	75	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$118,392.79	$2,486,248.61	$2,486,248.61

50-YEAR OLD NON-SPOUSE BENEFICIARY OF INHERITED IRA FULL WITHDRAWAL OF IRA REQUIRED WITHIN 10 YEARS

50 YEAR OLD NON-SPOUSE BENEFICIARY OF INHERITED IRA- FULL WITHDRAWAL OF IRA REQUIRED WITHIN 10 YEARS

A	B	C	D	E	F	G	H	I	J	K
Year	Age	Beginning Balance (Value at End of Prior Calendar Year)	Growth at 6%	Complete Distribution at Age 60	Income Tax on Distributions (37% Income Tax Rate)	Ending Balance (Value at End of Calendar Year, Assuming That Distribution is Made on Dec. 31)	Investment of Distributions (Column F Minus Column G)	After Tax Growth on Distributions Investment (5%)	Ending Balance of Distribution Investment Account	Total IRA Account and Required Minimum Distributions Investment Account Balance (Column G Plus Column J)
26	76	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$124,312.43	$2,610,561.04	$2,610,561.04
27	77	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$130,528.05	$2,741,089.09	$2,741,089.09
28	78	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$137,054.45	$2,878,143.55	$2,878,143.55
29	79	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$143,907.18	$3,022,050.73	$3,022,050.73
30	80	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$151,102.54	$3,173,153.26	$3,173,153.26
31	81	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$158,657.66	$3,331,810.92	$3,331,810.92
32	82	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$166,590.55	$3,498,401.47	$3,498,401.47
33	83	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$174,920.07	$3,673,321.54	$3,673,321.54
34	84	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$183,666.08	$3,856,987.62	$3,856,987.62
35	85	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$192,849.38	$4,049,837.00	$4,049,837.00
36	86	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$202,491.85	$4,252,328.85	$4,252,328.85
37	87	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$212,616.44	$4,464,945.30	$4,464,945.30
38	88	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$223,247.26	$4,688,192.56	$4,688,192.56
39	89	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$234,409.63	$4,922,602.19	$4,922,602.19
40	90	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$246,130.11	$5,168,732.30	$5,168,732.30
41	91	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$258,436.61	$5,427,168.91	$5,427,168.91
42	92	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$271,358.45	$5,698,527.36	$5,698,527.36
43	93	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$284,926.37	$5,983,453.73	$5,983,453.73
44	94	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$299,172.69	$6,282,626.41	$6,282,626.41
45	95	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$314,131.32	$6,596,757.73	$6,596,757.73
46	96	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$329,837.89	$6,926,595.62	$6,926,595.62
47	97	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$346,329.78	$7,272,925.40	$7,272,925.40
48	98	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$363,646.27	$7,636,571.67	$7,636,571.67
49	99	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$381,828.58	$8,018,400.25	$8,018,400.25
50	100	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$400,920.01	$8,419,320.27	$8,419,320.27

CHART COMPARING ROLLING OVER DECEDENT'S IRA VS. TAKING IT AS A BENEFICIARY



CHAPTER 5 – CHARITABLE PLANNING WITH IRA/PLANS – SPECTACULAR OPPORTUNITIES PROVIDED BY THE SECURE ACT

I. Charitable Coordination of IRA/Plan Beneficiary Designations and Distributions

The following discussion is based upon situations where a Plan Participant dies after 2019, although much is the same for Plan Participants who die before 2019.

Clients with charitable aspirations will be well served by advisors who understand how the IRA/Plan rules interact with charitable income, gift, and estate tax planning.

With the exception of the $100,000-per-year Qualified Charitable Distribution which applies to Plan Participants who have reached the age of 70½, the transfer of IRA/Plan investments to charities will trigger ordinary income to the Plan Participant, which may or may not be offset in whole or in part by a charitable deduction, based upon the charitable deduction limitation rules. The Qualified Charitable Distribution allows Plan Participants to have up to $100,000 of their Required Minimum Distributions payable directly to a public charity. Such payment will count as a Required Minimum Distribution to the extent of the amount of the payment. This law was not changed as a result of the SECURE Act, and Plan Participants who have reached the age of 70½ can continue to take advantage of the Qualified Charitable Distribution technique, notwithstanding that the Required Beginning Date age was increased to age 72; however, if deductible contributions to the IRA/Plan are made after the Plan Participant reaches age 70½, the $100,000 limitation on Qualified Charitable Distributions is reduced by the aggregate amount of such contributions.

For example, if a Plan Participant reached the age of 70½ in 2020 and made a $5,000 deductible contribution to her IRA in each of 2021 and 2022 and makes her first Qualified Charitable Distribution in 2022, then the maximum Qualified Charitable Distribution allowed in 2022 would be $90,000. If she makes a $4,000 deductible contribution to her IRA in 2023, and no Qualified Charitable Distribution until 2024, then the deduction otherwise allowed for her Qualified Charitable Distribution made in 2024 likewise will be reduced by $4,000. If she makes no further IRA contributions after 2023, then future Qualified Charitable Distribution will be completely deductible up to $100,000 per year after 2024.

Taxpayers who plan on making Qualified Charitable Distributions may wish to make contributions after age 70½ to a Roth IRA, because the above reduction of the charitable deduction does not apply to Roth IRAs because contributions to Roth IRAs are not deductible.

Because an IRA/Plan typically consists of built-up ordinary income tax when distributions are made, it is therefore usually more efficient to have an IRA/Plan transferred directly to charity upon death.

One or more charities can be named as direct IRA/Plan distribution beneficiaries, based upon set dollar amounts, percentages of value, or formulas whereby the amount or percentage of the distribution from the IRA or Plan to the charity is determined based upon other factors, such as, for example, being based upon the lesser of (a) the amount held in the particular IRA/Plan; (b) a set dollar amount; or (c) a set percentage of all of the person's assets. For example, the following disposition language can be used: "I give the Salvation Army the lesser of (a) the amounts held under this IRA account; (b) $1,000,000; or (c) 20% of my entire adjusted gross estate."

When a charity is named as one of a number of beneficiaries under a trust receiving IRA distributions, it will typically need to be paid out in full or otherwise eliminated as a beneficiary before the September 30th following the year of the Plan Participant's death so that the individual beneficiaries will have the ability to receive distributions by delaying payment until the December 31st of the 10th calendar year following the year of death of the Plan Participant, or based upon the life expectancy of an Eligible Designated Beneficiary, as described in Chapter 3, Section 2 of this Handbook where the Plan Participant has died before 2019, and as described in Chapters 7 and 8 where the Plan Participant dies after 2019.

If the trust is a Conduit Trust that requires that IRA/Plan distributions are to be paid to a Designated Beneficiary for Required Minimum Distribution purposes, then there is no problem from a Required Minimum Distribution rules standpoint with a charity being a discretionary beneficiary that would receive other assets from the trust, so long as all IRA/Plan distributions are distributed to the individual Designated Beneficiary, pursuant to Treasury Regulation Section 1.401(a)(9)-5, A-7(c)(3), Example 2, which reads as follows:

> **<u>EXAMPLE 2</u>**
>
> ***(i) The facts are the same as Example 1[87] except that the testamentary trust instrument provides that all amounts distributed from A's account in Plan X to the trustee while B is alive will be paid directly to B upon receipt by the trustee of Trust P.***

[87] The facts in Example 1 are as follows: Employer M maintains a defined contribution plan, Plan X. Employee A, an employee of M, died in 2005 at the age of 55, survived by spouse, B, who was 50 years old. Prior to A's death, M had established an account balance for A in Plan X. A's account balance is invested only in productive assets. A named a testamentary trust (Trust P) established under A's will as the beneficiary of all amounts payable from A's account in Plan X after A's death. A copy of the Trust P and a list of the trust beneficiaries were provided to the plan administrator of Plan X by October 31 of the calendar year following the calendar year of A's death. As of the date of A's death, the Trust P was irrevocable and was a valid trust under the laws of the state of A's domicile. A's account balance in Plan X was includible in A's gross estate under Section 2039.

> ***(ii) In this case, B is the sole designated beneficiary of A's account in Plan X for purposes of determining the designated beneficiary under section 401(a)(9)(B)(iii) and (iv). No amounts distributed from A's account in Plan X to Trust P are accumulated in Trust P during B's lifetime for the benefit of any other beneficiary. Therefore, the residuary beneficiaries of Trust P are mere potential successors to B's interest in Plan X. Because B is the sole beneficiary of the testamentary trust's interest in A's account in Plan X, the annual required minimum distributions from A's account to Trust P must begin no later than the end of the calendar year in which A would have reached age 70½, rather than the calendar year immediately following the calendar year of A's death.***

When leaving a portion of an IRA/Plan through a trust, to charity always define the gift as a fraction of the IRA/Plan, rather than a pecuniary portion (fixed dollar amount) to avoid possible triggering of income tax at the trust level. This was the IRS's position in Chief Counsel Advice (CCA) 200644020, which concluded that the satisfaction of a pecuniary charitable obligation caused a trust to receive an immediate economic benefit by funding with property upon which neither the Trust or the Decedent had "previously paid income tax which is a [taxable] disposition."

Alternatively, a "transfer pursuant to the right to receive such amount by reason of the death of the decedent or by bequest, devise, or inheritance from the decedent"[88] does not trigger income tax on the disposition. Therefore, the transferring entity is not taxed; instead the beneficiary pays the tax when a distribution is made. Since the distribution would be made to a charitable entity, no tax would be owed.

The charity selected may be one or more existing charities, or a family foundation or other "to be formed" charity that will need to be in existence by September 30 of the year following the death of the Plan Participant, for the reasons set forth above. This may be done under the revocable trust of the Plan Participant, or through the Plan Participant's estate by means of being set forth under his or her last will and testament. It is noteworthy that a trust and an estate may be treated differently in that an estate receives a deduction for amounts "permanently set aside" or paid, whereas a trust only receives a deduction for amounts paid if the original trust instrument specifically provides the Trustee with the power to make distributions to charity.[89]

It is important to expressly provide under the trust instrument or last will and testament of the Plan Participant that the income from the retirement plan or any other income under the assets of the Plan Participant's trust or estate is authorized to be used by the fiduciary to satisfy the devise to or for the benefit of the charity in order to ensure that the federal income tax charitable deduction applicable to trusts and estates under Subchapter J of the Internal Revenue Code will apply to the greatest extent possible.

[88] CCA 2006-44020.
[89] I.R.C. § 642(c)(2).

Sometimes it will work best to name one or more individuals and/or a trust or trusts as primary beneficiaries of the IRA/Plan, and to name a charity or charities as contingent beneficiaries, so that after the Plan Participant's death it can be decided whether it is best to have the Primary Beneficiaries disclaim to allow the charity or charities to be paid directly from the IRA/Plan.

For example, a high tax bracket individual beneficiary may prefer to receive IRA/Plan distributions over time, while making an immediate charitable contribution of up to one-half of the individual's adjusted gross income, in order to receive a personal tax deduction while satisfying the intentions of his or her parent or grandparent.

Many affluent families establish private foundations to be managed by their children, and then name their children as beneficiaries of IRA/Plan accounts, with the foundation being an alternate beneficiary. Under the estate and gift tax laws, a child cannot successfully disclaim any asset that he or she would have a power of direction over.[90]

The same rule would apply if the disclaimer is to a charitable remainder trust, gift annuity arrangement, or charitable lead trust when the disclaimant is a beneficiary or trustee thereof.

It should be possible, however, to name a foundation where the legal mechanisms will require that the disclaiming person will have no right of direction or control over the amounts disclaimed or the proceeds thereof, and such a limitation can be implemented after the death of the IRA/Plan Participant, as long as it occurs before the disclaimer is made.

See Appendix B for sample language for a charitable foundation under estate or trust to receive IRA distributions.

It should also be possible to name a donor advised fund as an alternate beneficiary for an individual beneficiary who may disclaim, even where the disclaimant is an advisor to the fund, because legally an advisor cannot "direct" the distribution of donor advised fund assets, notwithstanding that the fund sponsor almost always does exactly what the appointed family advisor requests as far as holding assets, investing them, and making distributions to public charities.[91]

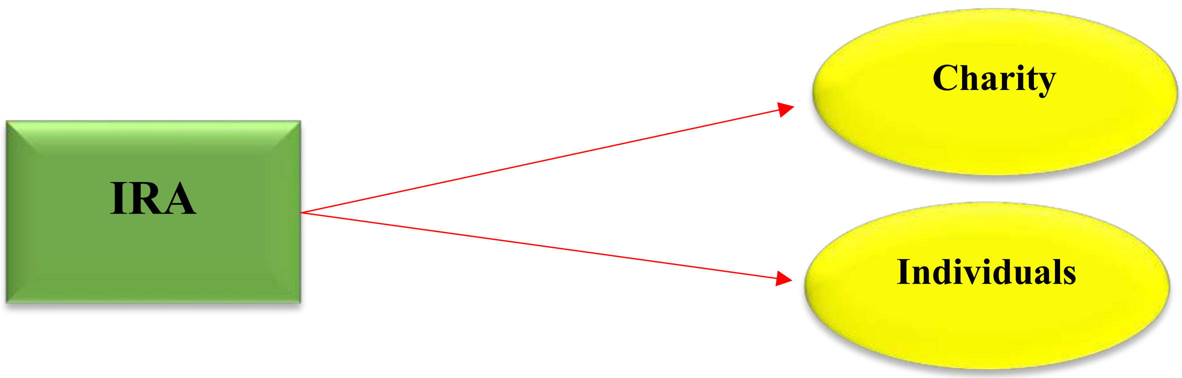
Sometimes IRA/Plan funds are to be received by an estate or trust, and may, in turn, be paid to a public or private charity. In this event, the distributable net income rules will apply to determine the timing of income and deductions and can be quite complicated. Most fiduciaries will prefer to have the IRA/Plan distribute the funds directly to the charity, or at least assure that the charity receives the funds in the same year that the trust or estate receives them from the qualified plan. See Section 7.4 of Natalie Choate's book *Life and Death Planning for Retirement Benefits* for an excellent discussion in this area.

PLR 200741016 blessed a planning alternative called the CHIRA™ ("charitable IRA"). Under a CHIRA™ an individual loans IRA assets to a charity, and the charity purchases

[90] See I.R.C. § 2518 and PLR 200522012.
[91] See PLR 200518012.

life insurance on the life of the Plan Participant. The life insurance serves as collateral in case the Plan Participant dies prior to the repayment of the loan. The amount loaned to the IRA recognizes no income tax, and at the death of the Plan Participant the charity receives the proceeds of the life insurance minus any outstanding loan balance. The Plan Participant can then either leave the remainder of the IRA to his or her family, or to the charity.[92]

SCENARIO D – PERCENTAGE TO CHARITY/PERCENTAGE TO INDIVIDUALS



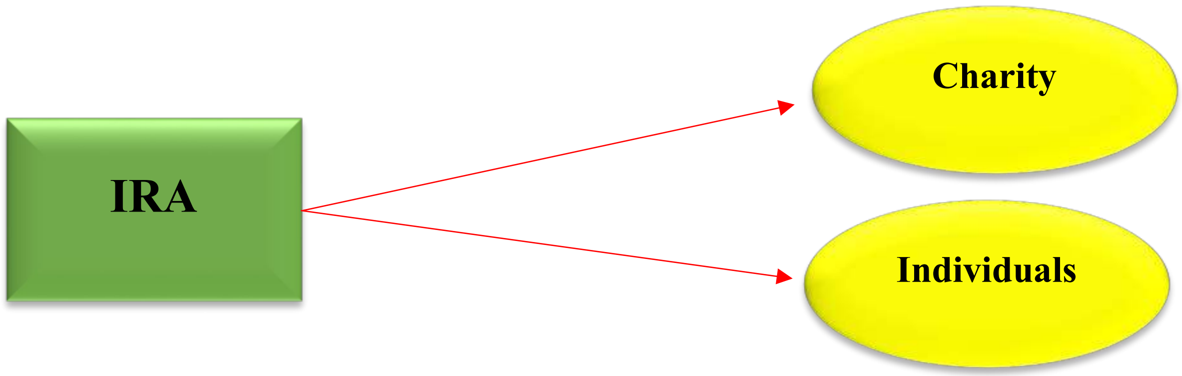
IRA goes in equal shares, percentages, or fractional shares to charity and individual beneficiaries; i.e., "I name as beneficiary of my IRA A Charity and my two sons in equal shares."

1. No income triggered on transfer or payment to charity.

2. Portion of IRA passing to individuals will be subject to the 10-Year Rule unless paid to an Eligible Designated Beneficiary.

[92] For further discussion see Steve Leimberg's Charitable Planning Newsletter #129 (October 16, 2007) at http://www.leimbergservices.com/, written by Steve Leimberg.

SCENARIO E --
PECUNIARY (FIXED DOLLAR) AMOUNT TO CHARITY / REMAINDER TO INDIVIDUALS



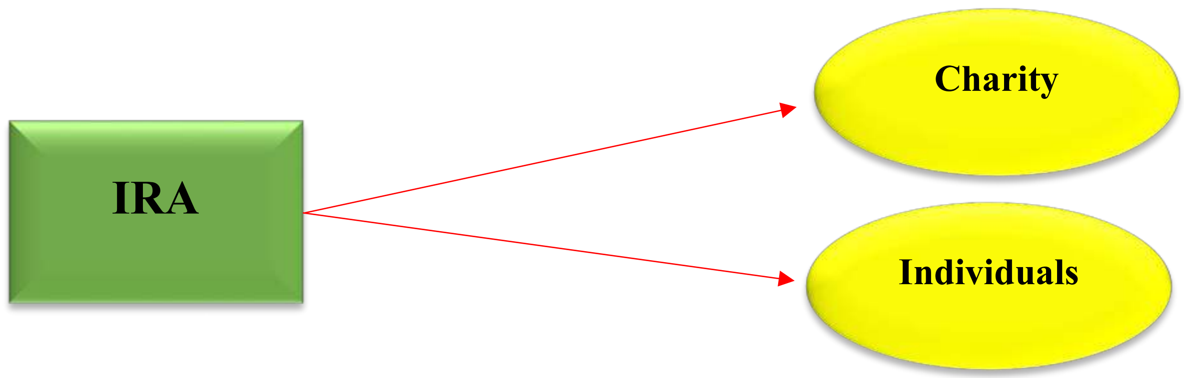
IRA goes dollar amount to charity, remainder to others; i.e., "$100,000 to Charity A, balance to my son."

1. No income triggered on payment to charity.

2. Portion of IRA passing to individuals will be subject to the 10-Year Rule unless paid to an Eligible Designated Beneficiary.

3. **NOTE** – If pecuniary amount is directed to charity via trust, then tax may be triggered at the trust level.

SCENARIO F – PECUNIARY TO CHARITY VIA FORMULA / REMAINDER TO INDIVIDUALS



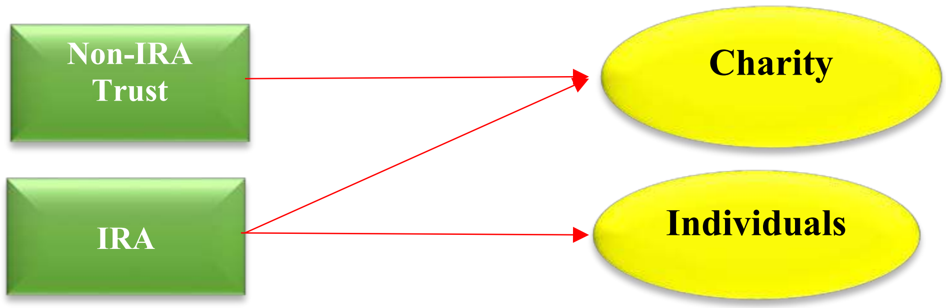
IRA leaves a pecuniary portion of the account to charity and remainder to individual beneficiaries; i.e., "$100,000 (computed via fractional formula) to Charity A; balance to my son."

1. Separate accounts are established with both shares sharing pro rata in the gains and losses until the date of ultimate distribution.

2. No income triggered on payment to charity.

3. Portion of IRA passing to individuals will be subject to 10-Year Rule unless paid to Elibigle Designated Beneficiary.

Scenario G – IRA Goes to Charity Only to Extent Charitable Disposition is Not Funded from Other Sources



IRA goes to charity to the extent that trust does not give the charity a full $1,000,000 and the rest to children.

1. If first paid to the Trust, and then to Charity, the Trust will receive an income tax deduction for amount paid to charity if (a) distribution was made pursuant to the governing instrument, and (b) payment was made out of income.

2. Portion of IRA passing to individuals will be subject to the 10-Year Rule unless paid to an Eligible Designated Beneficiary.

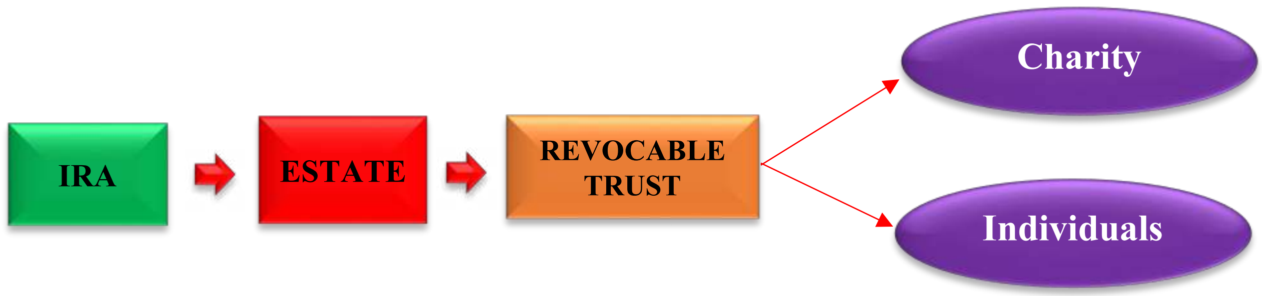
Scenario H – IRA Goes to Charity Only to the Extent that Charitable Disposition is Not Funded from Other Source

IRA is payable to the estate and last will and testament directs payments based upon one or more of the scenarios above.

1. Estate receives income tax deduction for amounts paid or set aside for charity.

2. When IRA is payable to the estate there is no designated beneficiary (even if transferred in kind to individuals by September 30th) thus either the 5-Year Rule or the At-Least-As-Rapidly Rule would apply for Required Minimum Distribution purposes.

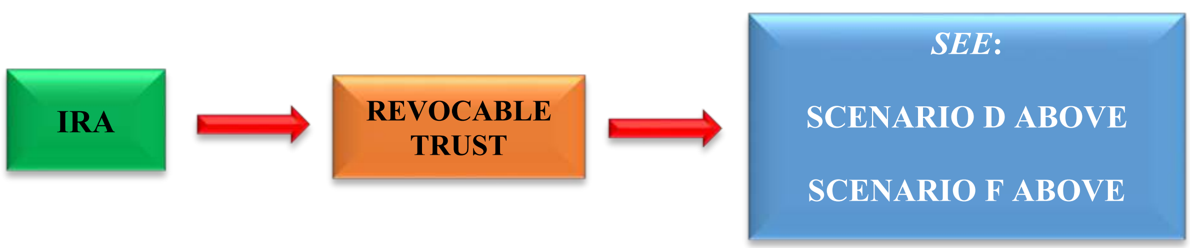
Scenario I –
Never-Ever-Ever Have IRA Payable to the Estate that is Payable to a Revocable Trust that Directs it to Charity



IRA is payable to the estate, which is payable to the Revocable Trust, which is payable under one of the scenarios above.

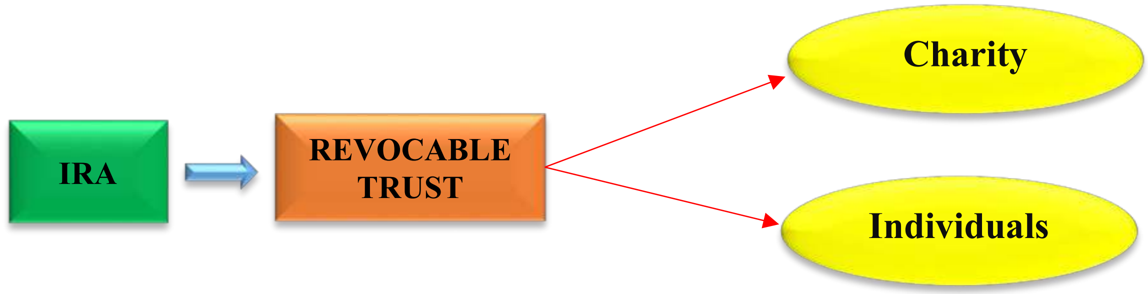
When IRA is payable to the estate, there is no designated beneficiary (even if transferred in kind to "See-Through" trust by September 30th); thus, either the 5-Year Rule or the At-Least-As-Rapidly Rule would apply for Required Minimum Distribution purposes.

Scenario J –
It is Okay for the IRA to be Payable to a Revocable Trust that Directs it to Charity, Unless Gift to Charity is Via Pecuniary Device



IRA is payable to the Revocable Trust, which directs it exactly as otherwise indicated above in Scenario D and F – the result is the same if the Revocable Trust is properly drafted,but *see* Scenario K below for whether charity is paid via a pecuniary devise through a trust.

SCENARIO K – ALWAYS DEFINE CHARITABLE GIFTS THROUGH TRUST AS A FRACTIONAL FORMULA RATHER THAN PECUNIARY



IRA is payable to Revocable Trust, which directs a pecuniary amount to charity, remainder to beneficiaries.

1. The pecuniary devise satisfies an obligation of the trust using property that no income tax has been paid upon, and is deemed to be a taxable distribution at the trust level.

2. When a gift is defined via fractional formula, the IRA is deemed to have been transferred intact, and the transferring entity is not taxed.

SCENARIO L –
IRA TO CHILD A – ALLOWS DISCLAIMER TO CHARITY

If Child A disclaims, no tax is triggered.

1. Charity cannot be private foundation over which the disclaimant is trustee or manager with power to direct the foundation's assets.

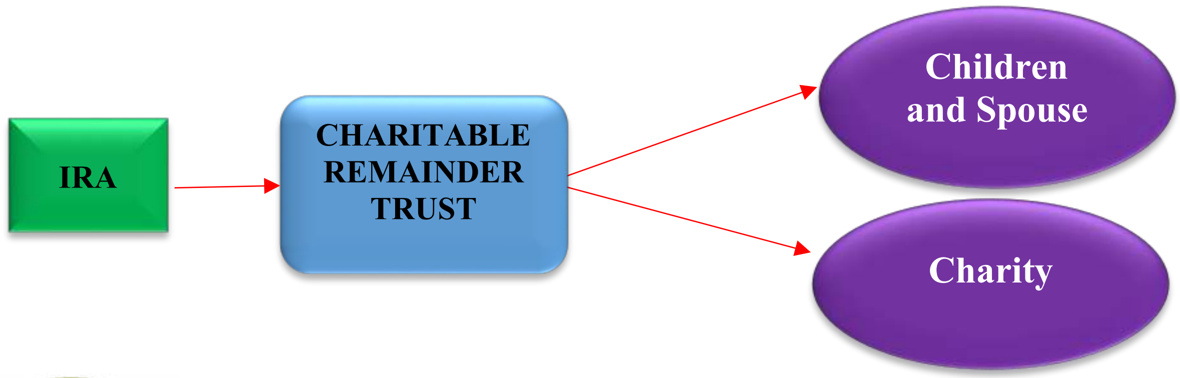
2. Disclaimants may recuse themselves from decision making power via a "Chinese Wall" provision to avoid disclaimer being deemed invalid.

3. Disclaimants should consider recusing themselves from decisions over donor-advised funds. One PLR has held that a disclaimer in favor of donor-advised funds does render disclaimer invalid due to the fact that the disclaimant is merely an advisor and cannot "direct" distributions. PLR 200518012.

Possible clause to facilitate the above:

"I intend to have $500,000 be paid to A Museum, located in Any City, Florida, provided that it is a 501(c)(3) organization and have been advised that it would be preferable to fund such devise from my IRA. I have therefore named my son Eric as beneficiary of my IRA B, with such charity being the alternate beneficiary. I request that my son determine whether it works best for federal income tax and estate tax planning purposes to disclaim such devise so that the IRA can pass directly to the Museum or to receive some or all of such devise as an inherited IRA and to make contributions to the Museum individually to receive income tax deductions. I recognize that this provision is not binding upon my son."

SCENARIO M–
IRA GOES TO CHARITABLE REMAINDER TRUST

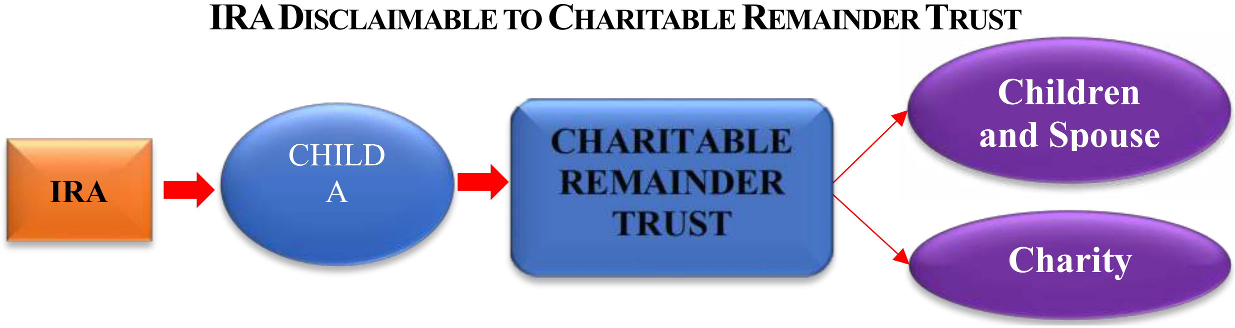


Payable to Charitable Remainder Trust which will make lifetime payments to Plan Participant's children and spouse, remainder to charity.

No income tax paid on benefits payable to Charitable Remainder Trust.

Distributions to Individuals will carry out taxable income on a "worst first" basis.

SCENARIO N–
IRA DISCLAIMABLE TO CHARITABLE REMAINDER TRUST



Payable to A, upon disclaimer to Charitable Remainder Trust which will make lifetime payments to children and spouse of Child A, remainder to charity.

No income tax paid on benefits payable to Charitable RemainderTrust.

Disclaimant cannot be an income beneficiary of the Charitable Remainder Trust unless the disclaimant is the Participant's Surviving Spouse.

Distributions to individuals will be carried out on a "worst first" basis.

II. Charitable Planning With IRA/Plans After The Secure Act

The 10-Year Rule which requires all assets held by the IRA/Plan to be paid out within ten years after the Plan Participant's death that will apply to most large non-spousal IRA dispositions under the SECURE Act has already made charitable planning a much bigger part of any conversation with charitably inclined individuals who have large IRA/Plans.

A great many families are already contributing to donor controlled or independent charitable organizations or have established arrangements to assure that charities will inherit upon specified circumstances.

These families may wish to reconsider how they will leave assets to charity, taking into account that most individuals who receive the benefit of non-spousal IRA inheritances will have to pay income tax no later than the eleventh year following the date of the Plan Participant's death, and that most trusts that receive benefits for such individuals will also be subject to the 10-year payout requirement if properly drafted.

The charitable alternatives include outright dispositions to independent charities, dispositions to donor advised funds and family foundations that can result in charitable accounts and investments that can be directed to charities by family members or friends over a long period of time, income tax-free dispositions to family foundations that can engage in private and public investments and activities and customized charitable conduct, with reasonable compensation paid to family members, and charitable remainder trusts which can be expected to provide well over 90% of value to family members and provide tax deferral over a stretch period that can be for twenty years, or longer, if based upon the life expectancy of one or more individuals.

Further, as discussed in more detail in Chapter 8, the 2022 Proposed Regulations made planning for charity more flexible than ever by providing that charities can be remote contingent beneficiaries of an IRA/Plan made payable to a See-Through Trust so long as the charity would only benefit if two individuals predeceased the Plan Participant.

The Preamble to the Proposed Regulations provides the following example to illustrate this rule:

> [A]ssume that an IRA names a see-through accumulation trust that requires the trustee to pay specified amounts from the trust to the employee's surviving spouse. Upon the spouse's death, the see-through trust is to terminate and the amounts remaining in the trust are to be paid to the employee's brother (who is not more than 10 years younger than the employee, and thus is an Eligible Designated Beneficiary). Further if the employee's brother survives the employee but predeceases the surviving spouse, then the amounts remaining in the trust after the death of the surviving spouse are to be paid to a charity.

> In that case, the charity is disregarded as a beneficiary of the employee because the charity could receive only amounts in the trust that are contingent upon the death of the employee's brother, whose only interest was a residual interest (that is, an interest in the amounts remaining in the trust after the death of the surviving spouse).
>
> In contrast, the charity would be treated as a beneficiary of the employee if the brother could receive amounts in the trust not subject to any contingencies or contingent upon an event other than the death of the surviving spouse (such as the surviving spouse's remarriage).

As further discussed in Chapter 8, the 2022 Proposed Regulations allow for a power of appointment to be exercisable in favor of charities without impacting the payout rules unless or until the power is actually exercised in favor of the charity.

Nevertheless, charitable planning is not for everyone. Ed Morrow points out the following in his LISI Income Tax Planning Newsletter #192 (February 18, 2020) at http://www.leimbergservices.com, entitled "Using BDOTs for Optimal Asset Protection and Income Tax Minimization After Passage of the SECURE Act:"

> Leaving traditional IRA funds to charitable remainder trusts and charitable annuities is only going to be palatable to taxpayers with strong charitable intent, who have little regard to the asset protection or sheltering of funds from estate tax for their beneficiaries. For those with taxable estates, the §691(c) deduction would likely go completely wasted by using a CRT![93] In short, extremely few people will ever strongly consider these more complicated estate planning structures over other options, such as simply carving out a charity as a direct beneficiary of a portion of an IRA without tethering them together with individual beneficiaries for life.

For clients who are charitably inclined, or who are open to the idea of leaving benefits to charity (or who may be incentivized by the tax savings from doing so), charitable planning can be very beneficial. Each of the above charitable planning alternatives is described in more detail as follows:

1. <u>Passing Benefits Directly to Charity</u>. The simplest and most direct method of charitable giving with IRA/Plan accounts is to make a 501(c)(3) charity the direct beneficiary of the IRA/Plan account on the beneficiary designation form.

[93] It is remotely possible that Florida law will not enable a creditor to reach amounts paid from an IRA or pension plan that have come through a Conduit Trust. *See In re Ladd* and *Gassman & Markham on Florida & Federal Asset Protection Law,* Chapter 8, Section C.

This will permit the IRA/Plan to pass directly to a bona fide Internal Revenue Code Section 501(c)(3) charity on the death of the Plan Participant, and very little will need to be done after death to facilitate this tax-free transfer.

An exception from an income tax standpoint would be that an Internal Revenue Code Section 501(c)(3) organization must pay income tax on any Unrelated Business Taxable Income, which would occur if the IRA/Plan owns an active trade or business that produces unrelated business taxable income. The vast majority of IRA/Plans do not have active trades or businesses that would generate unrelated business taxable income, but such entities may qualify for the Section 199A 20% deduction on such income if appropriate circumstances exist.

Another exception is that a private foundation or private operating foundation would be subject to a tax of 1.39% on its net investment income. Previously, this tax would either be 1% or 2% of net investment income depending on the operations of the private foundation, but the SECURE Act simplified this tax by making it apply at a flat 1.39% rate.

Natalie Choate has indicated that some charities or plan sponsors may find it problematic to have the applications filled out, and to make the payments directly to one or more charities, so that it may be easier to name the donor advised fund affiliated with the Plan Administrator, and to have family members or advisors then direct the monies to the selected charities. This indirect payment method should work fine, unless any person who has the authority to direct the charitable payments under the donor advised fund acts contrary to the wishes of the deceased Plan Participant.

If there is a complicated formula, then the plan administrator may not be comfortable complying with the terms of the trust agreement or will, or the instructions of the trustee or personal representative. For example, if a trust provides that "an amount equal to 15% of the net value of the trust will be payable to charity, or 40%, if I am not cohabitating with my present significant other," the plan administrator will not want to have responsibility for whether the proper amount was paid out. The alternative is to provide that "such amounts as are determined by the trustee to satisfy such provision shall be communicated to the plan administrator, as a devise of a specific dollar amount, and the plan administrator shall have no responsibility to determine whether such amount is accurate, and may rely upon a statement signed by the trustee of the trust in the presence of two witnesses and a notary public, or the order of a court of competent jurisdiction specifying the amount being transferred."

2. <u>Disclaimer to Charity</u>. The same income tax result discussed above can occur if the IRA/Plan is made payable to an individual or the trustee of a trust who disclaims the disposition within nine months of the Plan Participant's death, where the alternate beneficiary is one or more charities. This will be treated in exactly the same way as would apply if the charities were the direct beneficiary.

This can allow a high income tax bracket beneficiary, or a trustee acting for that beneficiary, to decide whether to accept an entire inherited IRA/Plan, or to allow some or all of the IRA/Plan to pass to a pre-named charity, donor advised fund, or charitable foundation.

For example, an IRA/Plan might be payable to a trust for the benefit of a child, his or her descendants, and designated charities, with the trustee having the power to disclaim the disposition. If the alternate beneficiary under the IRA/Plan beneficiary designation is the individual, then the individual may also elect to receive the disposition or disclaim it, and if the individual disclaims the disposition, then it can pass to a preselected charity named in the beneficiary designation as the second contingent beneficiary.

High income beneficiaries who may be inclined to donate more than the permitted percentage of adjusted gross income to charity may wish to speak with their parents, or other individuals who might leave IRA/Plan benefits to them, about these arrangements.

When disclaiming an interest in an IRA/Plan it is important that the disclaimant does not control the charity that will receive the funds as a result of the disclaimer. The disclaimant has to give up all control over the disclaimed interest. Pursuant to PLR 9008011, the disclaimant's spouse or other children who did not make the disclaimer were permitted to control the charity that receives the IRA/Plan proceeds. Alternatively, the PLR noted that the disclaimed property could be held in a separate account with the charity that the disclaimant has no control over.

Further, if the disclaimer results in the IRA/Plan proceeds going to a charitable lead annuity trust, then the disclaimant is not allowed to be a beneficiary of the charitable lead annuity trust.[94] Distributions from an IRA/Plan to a charitable lead annuity trust will cause tax to be incurred in the year of the distribution, and the 5-Year Rule will apply, so it will almost never be recommended that an IRA be payable to a CLAT.

This Chapter discusses the use of multiple disclaimers to maximize flexibility for such arrangements. For example, the charitable individual may want to be able to have a trustee decide whether he or she will be the primary beneficiary of a trust that will receive all or part of the IRA distributions within approximately eleven years of the Plan Participant's death, or to be the lifetime beneficiary of a charitable remainder trust, or to have the benefit pass all or in part to charity.

3. <u>To an Estate or Trust That Provides for Charity</u>. This can be a somewhat complicated area, as further described below, but provides for the most flexibility and contingency planning.

[94] *Christiansen v. Commissioner*, 130 TC 1 (2008).

For example, a wealthy taxpayer may provide that his IRA/Plan will pass via his living trust to charity, but in an amount not exceeding 15% of the total net worth passing as the result of his death, or an amount sufficient so that his descendants receive at least $10,000,000. In addition, this individual may wish to permit his children, to serve as the independent trustees, to elect to have more go to charity from their separate shares, if they wish to do so. All of this can be provided under a trust agreement or last will and testament where the beneficiary of the IRA/Plan is the trust or the individual's estate. If the beneficiary of the IRA/Plan is the estate, then the IRA/Plan will have to be distributed in five years rather than ten years.

In the past, having an IRA/Plan payable to an estate was a bigger problem because the beneficiary could potentially have received the IRA/Plan amounts over his or her lifetime, but the primary negative after the SECURE Act is that all of the IRA/Plan assets must be distributed in five years, in addition to being vulnerable to the claims of creditors. In addition, the 2022 Proposed Regulations provide even more flexibility as discussed in Chapter 8 by allowing charities to be permissible appointees under a power of appointment, and also contingent beneficiaries under an Accumulation Trust (a Tier III Beneficiary), without impacting the payout rules that would otherwise apply.

If an IRA/Plan is left to the decedent's estate and the decedent leaves a Surviving Spouse that is the sole beneficiary of the decedent's estate, then the Surviving Spouse could potentially be treated as the Designated Beneficiary of the IRA/Plan. Many companies managing IRA/Plan accounts will require a private letter ruling before rolling the IRA/Plan monies into an inherited IRA for the spouse, but this can be a costly process. For many individuals, it will not be worthwhile to incur the expense of obtaining a PLR/Plan simply to stretch the annuity over the Surviving Spouse's lifetime, since the filing fee alone for such a PLR as of 2020 could be up to $30,000. Fortunately, an IRA/Plan may be transferred after death to a new custodian that may be more willing to honor the beneficiary designation with a court order, which will be much less expensive and time consuming than obtaining an IRS Private Letter Ruling.

Other disadvantages of naming an estate as beneficiary are described below.

As a general overview, a great many Plan Participants will prefer to have formulas and conditions that will apply to determine if and how much charities will receive under an estate plan, and will not want to be inconvenienced with having direct or somewhat complicated beneficiary designation arrangements that might run amuck if and when they ever change advisors, or update beneficiary designations. By having the beneficiary of an IRA/Plan be a trust that is established during the life of the Plan Participant, or as a testamentary trust upon his or her death, the specific formulas and contingencies, along with customized language that can provide limitations and detailed instructions to carry out charitable and non-charitable intentions can be provided in the trust document, and can be modified and developed in future codicils and amendments without having to change the beneficiary designation.

When an IRA/Plan is payable to an estate or trust, the income is carried out into the estate or trust, but the estate or trust will receive up to a 100% income tax deduction under Internal Revenue Code Section 642(c), if amounts equal to the amounts that passed from the IRA/Plan pass directly to charity within the applicable deadline and the trust contains the appropriate provisions.

In order to meet the above deadline, a trust must make the applicable distribution before the end of the tax year following the year in which the IRA/Plan distribution is received.[95]

For an estate, the distribution will be considered as having been made by such deadline, as long as the amounts received by the estate are "set aside" in a proper manner, and eventually paid to charity before the estate is closed. That is the one advantage of making the estate of the Plan Participant the beneficiary of an IRA/Plan account that will be going in whole or in part to charity.

For the 642(c) deduction to apply, it is crucial that the will or trust document specifically authorizes or requires the trustee or personal representative to make payments to charity. It is not sufficient for this provision to be added by a trust protector or court order after the death of a testator or once a revocable trust or other trust becomes irrevocable. This rule does not apply to income passing through an estate or trust from an IRA/Plan to charity.

It is important to note that money received from an IRA/Plan is not subject to the 3.8% Medicare Tax, but if IRA/Plan proceeds are distributed to a trust, the trust may eventually hold undistributed net investment income, generated from the investment of such funds, which could be subject to the 3.8% Medicare tax.

Other disadvantages can include loss of the ability to use the 10-Year Rule, if the estate does not "pour" the IRA or pension benefit into a trust or to a person that would so qualify, or the loss of a lifetime payout for a disabled or chronically ill individual where the estate does not "pour" the benefit to an Accumulation Trust that would qualify for such an individual, or to the individual themselves.

4. <u>When Does the September 30 After Year of Death Rule Impact the Above Planning?</u> This book provides numerous examples of when charities and other non-individuals must not be beneficiaries, or in some cases even potential future beneficiaries, of trusts that would otherwise qualify for a lifetime payout for a Surviving Spouse, or certain other categories of Eligible Designated Beneficiaries,[96] or at least the 10-Year Rule would apply.

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[95] Treas. Reg. Section 1.642(c)-1(b)(1).

[96] An individual not more than ten years younger than the Plan Participant, a disabled or chronically ill beneficiary, if the Plan Participant had reached his or her Required Beginning Date before death and the "Shadow Rule" applies, when the beneficiary is a minor child of the deceased Plan Participant, so that the Life Expectancy Rule may apply until the child reaches the age of majority, after which the 10-Year Rule would apply.

In these situations, the See-Through Stretch Trust rules can apply to the portions of distributions passing to separate, or, in some cases, combined trusts for the Designated Beneficiary, or plan benefit rights can pass directly through to such individuals or Gift to Minors Act accounts, or possible other vehicles for such individuals, as long as the charities and other Non-Persons[97] are completely paid out or otherwise eliminated as beneficiaries, so that they cannot receive anything after the September 30 of the year following the date of death of the Plan Participant.

Here are the primary circumstances that will apply under most estate and trust plans:

1. Pay a specified amount or percentage to charity shortly after the death of the Plan Participant.

    A. <u>Charitable Deduction Allowed When Charity Will Receive a Specific Amount or Percentage, Which Can Be Satisfied on or Before the September 30 Following the Date of the Plan Participant's Death.</u> In most cases, the trust or will is drafted to direct how much a charity or charities will receive. If it is not clear what portion of an estate or trust will pass to the charitable beneficiary or beneficiaries by September 30 following the year of the Plan Participant's death, then the trustee or personal representative may be able to set aside a "charitable share" subtrust to hold monies or other assets that will eventually be distributed to charity for up to two years following the Plan Participant's death. In order to take advantage of this provision with a trust, a Section 645 election must be made to treat the trust as part of the Plan Participant's estate.

       When some or all of such portion is distributed to charity within such two year period and the trust contains the appropriate language to direct a distribution to charity, then Internal Revenue Code Section 642(c) will apply, and there will be no tax on the amounts distributed from the IRA/Plan to that subtrust.

       This exception only applies to amounts that are set aside for the charitable beneficiary and not for any non-charitable beneficiaries.

    B. <u>The Interest Going to Charity or to Non-Charity Can Be Pecuniary or Fractional</u>. When the charitable and non-charitable interests are to be segregated or divided before September 30 of the year following the Plan Participant's death, the question as to whether the distribution is a pecuniary or fractional amount, which goes to charity or to the non-charitable beneficiaries will not matter. In other

[97] And in some situations, no person older than the applicable Designated Beneficiary.

words, it is fine to provide a pecuniary disposition (e.g., the charity or non-charity will receive $400,000, and the other parties will receive the remainder of the trust or estate assets), or a fractional (e.g., the charity or non-charity will receive 18% of the greater of the net amount of assets passing from the IRA/Plan or 8% of the total net value of the trusts passing upon death, with the remaining assets going to the charity or non-charity beneficiaries).

Special care should be taken when making the trust the beneficiary of an IRA/Plan. Generally, the trust can have a charitable beneficiary as a fractional beneficiary without causing any problems, but having a charity as a pecuniary beneficiary may cause negative tax consequences. It is important that the trust document provide the trustee with the ability to allocate items of income to the charitable beneficiary and to specifically provide that the IRA/Plan proceeds will be used to fund the charity's interest in the trust, to the extent possible.

If such specific language is not included, then there may be an issue with gain being recognized by the trust or allocated to the non-charitable beneficiaries. For example, if the trust does not have the proper provisions and an IRA/Plan was paid out to the trust in the amount of $3,000,000, and the trust directed that $3,000,000 would be paid to a charitable beneficiary and that $3,000,000 would pass to a non-charity, then the trust may receive only a $1,500,000 Section 642(c) deduction based upon the premise that the IRA/Plan proceeds and non IRA/Plan assets were each paid one half to the charity and one half to the non-charitable beneficiary.

Due to the risk mentioned above, it makes good sense to provide in the "boilerplate" of all trust documents that any time that monies are to be received from an IRA/Plan, such proceeds should go into a separate subtrust under the trust agreement, which will be used to fund any charitable devises before having such funds used for any non-charitable beneficiaries, and that the Trustee of such subtrust would be permitted and encouraged to distribute only to charity in one tax year, and only to the non-charitable beneficiaries or trusts for their benefit in a subsequent tax year, if recommended by a tax advisor.

2. <u>Charitable Gift Annuities</u>.

A Charitable Gift Annuity is an annuity contract issued by a charity to an individual or individuals under which the charity promises to make payments to such individual or individuals based upon a payment schedule or formula over their lifetime. A Charitable Gift Annuity cannot be for a term of years or have any minimum term of years that would apply, even if the individual dies almost immediately after the annuity is funded.[98]

Many families will therefore put inexpensive term life insurance into place to help offset the risk of the early death of the individual or individuals whose lives are used.

The tax law permits a donor who buys a Charitable Gift Annuity contract to receive an income tax deduction based upon the excess of the amount of money or other assets given to the charity over the actuarially calculated value of the annuity contract payment rights, which is typically 50% of the amounts contributed. The American Council on Gift Annuities ("ACGA") provides suggested maximum payout rates for Charitable Gift Annuities and uses a target residue of 50% of the contribution that is made as consideration for the gift annuity. Under Internal Revenue Code Section 514(c)(5)(A), the charity is required to be expected to retain at least 10% of the present value of the Charitable Gift Annuity, assuming that the payments will be made for the life expectancy of the annuitant, and the growth assumptions described below are accurate.

The ACGA recommends that charities perform their own calculations to ensure that the non-charitable person or entity purchasing the Charitable Gift Annuity will receive at least a 10% charitable deduction and recommends that the charity will expect to receive at least 20% of the present value of the annuity. The charity issuing the annuity can take compounding growth into account in the event that the annuity payments will not start until a future date. In such a case, the charity would need to make an assumption of what the compounding rate would be. As of February of 2020, the compounding rate suggested by the ACGA is 3.25%, which assumes that the annuity assets will grow at a rate of 4.25% with a 1% assumed annual expense ratio.

For example, a donor with appreciated real estate with a fair market value of $100,000 and a cost basis of $10,000 may give the property to charity in exchange for a lifetime annuity that will pay her $2,500 a year for the rest of her life, and may receive a $50,000 income tax deduction.

The charity normally will take the risk that it can afford to make the annuity payments for the entire lifetime of the named beneficiary or beneficiaries, or may buy a commercial annuity contract in the name of the charity that can be collateral for the obligation to make the payments to the donor's beneficiaries. If such a commercial annuity contract is purchased by the charity, then the charitable deduction of the donor will be based upon the excess of the amounts paid to the charity over the cost of the commercial annuity contract that is purchased by the charity, in lieu of using the IRS provided actuarial amounts.

[98] *Charitable Gift Annuity*, Planned Giving Design Center, by Marc Hoffman, May 18, 2011.

If the charity is able to purchase a commercial annuity for the annuitant, then there is no real risk to the charity.

Some charities do not enter into Charitable Gift Annuities out of concern that they will not be able to satisfy the annuity payments, or that the annuitant will outlive their life expectancy, resulting in the charity receiving less of a benefit from the Charitable Gift Annuity.

The income tax treatment of payments made from a Charitable Gift Annuity to a non-charitable beneficiary is not clear. The IRS may take the position that the income tax basis of a Charitable Gift Annuity received in exchange for an IRA/Plan should be considered to be zero, so that all payments received by the non-charitable beneficiary will constitute ordinary income. However, some practitioners believe that the amount paid to the charity on the death of the Plan Participant will constitute basis to be applied over the scheduled number or expected number of lifetime annual payments to be received under Internal Revenue Code Section 72.[99]

It appears clear under the income tax rules that an IRA/Plan made payable directly to a charity that agrees to issue a Charitable Gift Annuity to a deceased Plan Participant's spouse, child or other individual will not be subject to income tax in the estate of the Plan Participant, or to the individual who receives the right to receive the charitable annuity payments. PLR 200230018 appears to be the only real guidance issued by the IRS in relation to how the income from a Charitable Gift Annuity will be taxed to the non-charitable beneficiary. In this PLR, the IRS indicated that the income in respect of the decedent would be "taxable" to the charity, although it seems clear that the charity will not have to pay tax on the income that it receives.

If the income in respect of decedent ("IRD") is "taxable" to the charity, then it would follow that the ordinary income character of any IRA/Plan made payable to the charity in exchange for the Charitable Gift Annuity would not carry out to the annuitant. Even though the IRD is "taxable" with respect to the charity, the charity will not pay taxes on such amount because it is a tax-exempt organization. Many tax professionals assume that 100% of the payments made to the annuitant would be subject to ordinary income tax as if the annuity had no "cost basis," although it seems likely that the amount of the annuity that passes to the charity should be considered to be the "cost basis" that can be considered to reduce the ordinary income component of each payment received up until the recipient/annuitant reaches his or her life expectancy.

In the event that the IRD is not passed to the non-charitable beneficiary through the annuity payments, then the non-charitable beneficiary may receive more after-tax

[99] Under Section 72, basis is normally allocated equally between each of the annual payments that are scheduled to be made until the original life expectancy of the beneficiary has been reached, with any payments received thereafter being treated as 100% ordinary income.

dollars than if the decedent had simply purchased an annuity with his or her IRA/Plan assets, in addition to benefiting a charity.

For example, a Plan Participant leaves a $1,000,000 IRA to charity in exchange for a charitable gift annuity for his daughter, who is 50 years old at the time of his death. In this case, the daughter would receive $37,000 per year from the charity for life and the estate would receive a charitable estate tax deduction of approximately $200,000, but would not receive a charitable income tax deduction. The present value of the annuity might be approximately $800,000 if the charity will agree to an 80/20 value split (the normal split in the industry is 50/50). A 50-year-old has a life expectancy of 34.2 years, meaning that the daughter can expect to receive approximately $1,265,400 over her remaining lifetime, and will receive more if she outlives her life expectancy, but less if she dies early.

Another benefit in the above example is that the beneficiary is receiving the income over her lifetime, which increases the chances that payments will be taxed at lower tax brackets. The daughter will be considered to be receiving $13,000 a year of income and $24,000 a year of basis recovery until after the 34th year, and then the entire $37,000 per year will be treated as ordinary income.

The IRS may take the position that the entire $37,000 per year should be treated as ordinary income during the daughter's life, but there does not appear to be substantial support for either position.[100]

The charity's receipt of the IRA/Plan amounts are not considered to be unrelated business taxable income, even if the charity is "in the business" of selling Charitable Gift Annuities to support its charitable purposes.

The recipient of the annuity payments may be able to apply the cost of the annuity that is paid from the IRA/Plan as basis, as if the IRA/Plan amount that was used to purchase the annuity consisted of after-tax dollars, although it seems likely that the IRS will claim that the income tax basis of an annuity received in exchange for an IRA should be considered to be zero, so that all payments received will constitute ordinary income.

In the event that the IRD is not passed to the annuitant through the annuity payments, then the annuitant may receive more after tax dollars than if the decedent had simply purchased an annuity with his or her IRA assets, in addition to benefiting a charity.

This issue was discussed in Leimberg Information Services Charitable Planning Newsletter #292 by Lawrence Katzenstein.

In order to receive an estate tax charitable deduction for the charitable element of a Charitable Gift Annuity arrangement, the charity receiving the IRA distribution

[100] See an excellent article written by Lawrence Katzenstein at LISI Charitable Planning Newsletter #292 (February 10, 2020) at http://www.leimbergservices.com.

must be obligated to issue a defined Charitable Gift Annuity effective on the date that the Plan Participant died.

This requirement can be satisfied by having an agreement set up in advance with a charity, or by having clearly defined language in a beneficiary designation that specifies exactly how the payments for the annuity will be calculated, so that the deduction amount is set in stone, and having the IRA made payable to a charity that accepts the terms set forth in the beneficiary designation. For example, the beneficiary designation might indicate that "ABC Charity, if ABC Charity agrees to issue a lifetime annuity that will pay my surviving spouse Edna the amount of 6.2% of the value of the IRA assets that are actually paid to ABC Charity for her lifetime, beginning one year after my date of death, provided that such percentage shall be changed to the extent necessary so that the payment amount will satisfy all requirements necessary to enable such Charitable Gift Annuity to qualify so that no income tax is paid by my estate, revocable trust, or beneficiaries upon the issuance of such annuity by ABC Charity, and if ABC Charity is unable or unwilling to accept such disposition and provide such annuity contract then BCD Charity will receive such IRA, subject to the same conditions and requirements as set forth above to apply."

The above language may work to create a Charitable Gift Annuity and to have the income in respect of a decedent allocated to the charity. There is a chance that the charity may be uncomfortable with such language because the charity may not want to affirmatively take the position that no income tax will be paid by the estate, revocable trust or by beneficiaries upon the issuance of the annuity. This is why it is more prudent to enter into an agreement with a charity before the death of the Plan Participant, so that the charity will be bound to honor the terms of the Charitable Gift Annuity upon the Plan Participant's death.

3. <u>Charitable Remainder Trusts.</u> The topic of charitable remainder trusts has caused the tax and estate planning community to dust off years of coverage of this under-utilized and commonly misunderstood income tax deferral tool in order to replicate, and in some cases, exceed the utility of a lifetime payout for the benefit of one or more beneficiaries who would have otherwise been subject to payment of income tax on the IRA/Plan distributions before the 11th year following the death of the Plan Participant or beneficiary.

By its simplest terms, a charitable remainder trust is a trust that is authorized under Internal Revenue Code Section 644 and Treasury Regulations Sections 1.664-1 through 1.664-4 to receive and hold income tax-free, and to allow for deferral of recognition of such income until distributed on a "worst first" basis.

For example, a charitable remainder annuity trust might receive $2,000,000 from an IRA and be required to pay a fixed annual amount of $100,000 per year for 20 years to its individual beneficiary.

Assuming that the $2,000,000 is invested in stocks which yield only capital gains and qualified dividends that are taxed at the 20% bracket, the first 20 payments from the trust will carry ordinary income out to the beneficiary, and remaining payments will carry any capital gains and qualified interest out, so that the beneficiary is taxed at whatever rate applies to such categories of income in the year of receipt.

The deferral of income tax allows income to be accumulated without tax being imposed while the assets are held in the charitable remainder trust. Additionally, the beneficiary will receive less per year over a term of years in order to reduce the marginal tax rate, assuming that the beneficiary would not otherwise be in the highest marginal tax bracket.

One advantage of a charitable remainder annuity trust is that the payments made may be protected from creditors of the beneficiary, if the beneficiary resides in a state or other jurisdiction that provides creditor protection for annuity amounts received.[101]

The other advantage of a charitable remainder annuity trust is that the beneficiary will know exactly how much money he or she will receive each year, but assuming normal growth and investment results, the individual beneficiary or beneficiaries will receive less, and the charitable remainder interest going to the charity or charities will be significantly greater than what will normally apply under a charitable remainder unitrust. On the other hand, if the assets do not return an amount in excess of the Section 7520 rate, the charity's remainder interest would be depleted before the beneficiary's annuity amount is reduced.

It is noteworthy that the trustee and beneficiary of a charitable remainder trust can be given the power to designate and change the charitable beneficiary or beneficiaries, so long as the "selector" will not be able to control the monies or other assets that flow to the charity from the charitable trust. This will not prevent the individual with the selection power from being on the board of a private foundation or other entity that receives such proceeds, as long as the charitable entity's account or accounts that are funded with the proceeds, and the income and benefits associated therewith, are not controlled by such individual. This is similar to the restrictions that apply if the individual is the beneficiary of an IRA/Plan and has disclaimed all or part of the IRA/Plan to charity.

With a charitable remainder unitrust, the non-charitable beneficiary or beneficiaries will receive a percentage of the fair market value of the trust assets in cash or in kind from the trust each year, based upon the fixed annual percentage established upon formation, which will typically be based upon formula language which provides that the percentage will be the highest percentage permitted, so that the

[101] In the Florida case of *In Re Mart,*, Mr. Mart sold assets to a trust that he established for his daughter in exchange for the right to receive an annuity payment. The Bankruptcy Court held that Florida law provided for the annuity payment right to be exempt from creditor claims in bankruptcy.

expected remainder disposition for charity will be at least 10% as measured under the IRS Publication Actuarial Valuations Version 3(b). There are multiple tables that will provide the remainder value when the trust is based upon a single life, two lives, or for a term certain.

The amount paid to the non-charitable beneficiary of the charitable remainder unitrust must equal at least 5%. If the beneficiary is too young, then it might not be possible to pay at least 5% to the non-charitable beneficiary. As of January 2020, a charitable remainder unitrust annual payment amount cannot be based on the life of a sole lifetime beneficiary who is under age 28.

As of January 2020, the following annual payout percentages will apply under the following circumstances to satisfy the 10% rule and maximize the percentage paid out each year.

Length	Percentage
20-year term of years	10.87%
28-year-old’s life	5.08%
30-year-old's life	5.31%
40-year-old's life	6.92%
50-year-old's life	9.64%
60-year-old's life	14.90%

ON THE LIFE OF TWO PEOPLE	
Two 30-year-old individuals	Cannot distribute the required 5% or more amount
Two 39-year-old individuals	5.02%
Two 40-year-old individuals	5.13%
Two 50-year-old individuals	6.60%
Two 60-year-old individuals	9.10%

ON THE LIFE OF THREE PEOPLE	
Three 30-year-old individuals	Cannot distribute the required 5% or more amount
Three 40-year-old individuals	Cannot distribute the required 5% or more amount
Three 43-year-old individuals	5.02%
Three 50-year-old individuals	5.92%

The percentage must be the same each year and cannot fluctuate or increase annually in the same way as would apply for a charitable lead annuity trust or a private annuity arrangement.

In Private Letter Rulings 9710008, 9710009 and 9710010, the IRS ruled that charitable remainder trust payments cannot be made to a trust for the benefit of a grantor's child, unless the child is incompetent. This is also provided for in Revenue Ruling 2002-20, where the IRS approved a charitable remainder unitrust to pay an irrevocable trust for the benefit of an incapacitated individual. The general rule is that the charitable remainder unitrust payments that are to come out over the life expectancy of one or more individuals must be made directly to the individual or individuals, and not to a trust or other than directly, unless a beneficiary has special needs, as described below.

As mentioned above, a lifetime payout charitable remainder unitrust may permit payments to pass to a trust or trusts to benefit one or more special needs beneficiaries. This was permitted under Revenue Ruling 2002-20. This rule does, however, provide some planning advantage for the creation of special needs trusts that provide for discretionary payments to the beneficiary. It may be possible to create a special needs trust to benefit from a charitable remainder unitrust, and not distribute funds to the special-needs beneficiary due to the beneficiary's need to qualify for governmental assistance. This could potentially provide better creditor protection for the annuity amounts received from the charitable remainder unitrust.

<u>Advantages of Using a 20-Year Term</u>. In general, a charitable remainder unitrust may pay unitrust amounts to a second trust only for a term of 20 years or less. More specifically, a charitable remainder trust can be set to make payments for 20 years, without regard to life expectancy or survival of one or more beneficiaries, and the Trustee of a 20-year unitrust can have the discretion to "spray" the annual payments among one or more beneficiaries, or trusts for their benefit.

Further, a 20-year charitable remainder unitrust can be created for a beneficiary who is too young to have the charitable remainder unitrust payments based on his or her life expectancy.

If the beneficiary is too young to qualify for a charitable remainder unitrust to be based on his or her life expectancy by less than five years, then it may be possible to make the IRA/Plan payable to an irrevocable trust that will become a charitable remainder unitrust within five years after the death of the Plan Participant. Language should be added to the trust to make sure that if the beneficiary is still too young for a lifetime charitable remainder unitrust, that a term of 20 years will be used.

A charitable remainder trust that makes lifetime payments to two or more individual beneficiaries on multiple lifetimes, it can be divided into multiple trusts for the various non-charitable beneficiaries, with each trust receiving a pro rata portion of the trust's assets. This possibility is discussed in Revenue Ruling 2008-41, which states that a charitable remainder trust based upon two or more lives can be divided between the non-charitable beneficiaries with each trust being allowed to have its own trustee and investment strategy. The other provisions of the charitable remainder trust must continue to apply.

If a charitable remainder trust is divided into a separate trust for each non-charitable beneficiary, then upon the death of each non-charitable beneficiary the remaining assets of that individual's trust will be divided equally among the trusts held for the surviving non-charitable beneficiaries. Thus, the charity will still have to wait until the death of the last non-charitable beneficiary to receive the remainder. An exception to this general rule applies in divorce. If the charitable remainder trust is divided pursuant to a divorce, the trust assets will divide into separate trusts for each surviving ex-spouse beneficiary, but upon the death of each ex-spouse beneficiary, the remaining assets of the unitrust for that ex-spouse will go to charity and not to the unitrust held for the Surviving Spouse. This results in less value going to the non-charitable beneficiaries, and Revenue Ruling 2008-41 specifically states that no additional charitable deduction will be recognized. Spouses may want to consider dividing a Charitable Remainder Unitrust before filing an action for dissolution of marriage.

A more advanced and possibly advantageous type of charitable remainder unitrust is the NIMCRUT (which stands for Net Income with Makeup Charitable Remainder Unitrust), and a variety of NIMCRUT commonly used is the flip-NIMCRUT. These entities only make distributions to non-charitable beneficiaries to the extent income is received. If the NIMCRUT does not have income to distribute, the amount that otherwise should have been distributed in any given year could be "made-up" in future years.

A NIMCRUT may be used to provide for a small charitable income tax deduction in the year of contribution, and to delay payment of income taxes for over 15 years by having the NIMCRUT own an interest in an entity (e.g., an LLC taxed as a partnership or a disregarded entity). Until the entity distributes funds to the NIMCRUT, the NIMCRUT will not have any income to distribute to the non-charitable beneficiary. Once the decision is made to distribute monies to the non-charitable beneficiary, the entity can distribute cash to the NIMCRUT. Under Florida Statute Section 738.401, monies received from an entity will be considered to be income and can be distributed from the NIMCRUT. This provides the NIMCRUT with a way to control the amount the NIMCRUT is required to distribute.

Florida Statute Section 738.401 provides that any distribution in excess of 20% of the entity's value will be considered principal, which would not be eligible to be distributed from a NIMCRUT. Thus, it will take at least five years to fully distribute the make-up account and will likely take longer depending on the annual distribution percentage of the NIMCRUT. This problem is especially important to consider for older beneficiaries who have high annual payout percentages and a shorter life expectancy.

A Flip-NIMCRUT is a variation of the NIMCRUT which can "flip" to being treated as a regular NIMCRUT at some point in the future, at which point it will make standard annual Charitable Remainder Trust distributions to a non-charitable beneficiary. Once the flip-NIMCRUT becomes a regular Charitable Remainder

Trust it can start distributing principal to satisfy its annual distribution requirements. The use of this planning tool can allow the assets held by the NIMCRUT to continue to grow tax-free, due to the fact that charitable remainder unitrusts are exempt from income tax. Tax is only paid when funds are distributed to the non-charitable beneficiary. It is important to run projections for any specific beneficiary that may benefit from a NIMCRUT, because there are a number of variables that could make the NIMCRUT either more or less attractive.

For example, a beneficiary in a lower tax bracket would likely benefit more from a regular CRUT than an individual in a higher tax bracket, because the individual in the lower tax bracket would likely be pushed into a higher tax bracket in the event that such individual had to take large distributions from the IRA/Plan when the assets are distributed 10 years after the Plan Participant's death, whereas the regular CRUT can extend those payments over the beneficiary's lifetime. A high-income individual may already be in the highest tax bracket, and receipt of large amounts of income would not increase the applicable tax rate. It is important to take into account that once the NIMCRUT starts paying income to the non-charitable beneficiary, the payments will likely be relatively high in the initial years of payment, and then level out once the makeup account has been fully distributed.

Consideration also must be given to the age of the non-charitable beneficiary, because an older non-charitable beneficiary may not live long enough to receive the full value of the make-up account, which would pass to charity if not distributed to the non-charitable beneficiary. On the other hand, if the beneficiary is too young, the assets of the charitable remainder unitrust may grow at a rate that is higher than the distribution amount, meaning that significant assets will get trapped in the NIMCRUT, and will benefit charity rather than the non-charitable beneficiary.

It is also notable that the charitable remainder trust rules are very restrictive with respect to requiring that payments must be made directly to a non-charitable beneficiary or beneficiaries, and not to a trust for their benefit, unless the beneficiary is disabled, at least according to the IRS.

Sample calculations of the above strategies are available upon request by contacting the authors.

While a charitable remainder trust can allow the income from the IRA/Plan to be recognized over the beneficiary's lifetime, or 20 years, the Plan Participant should be cognizant of the possibility that the charitable remainder trust may be terminated early, based upon mutual consent of all beneficiaries, whereby the non-charitable beneficiary may receive a better economic arrangement than would otherwise be the case. Some taxpayers may request that the charitable remainder trust be drafted to prevent such early termination.

The calculation of what the non-charitable and charitable beneficiaries of a charitable remainder trust will receive upon early termination assumes that assets will grow at the artificially low Section 7520 rate, which favors the non-charitable beneficiary, and may make up for the fact that taxes will have to be paid earlier than would otherwise be the case. PLR 200208039 and PLR 200324035 included discussion regarding the non-charitable beneficiary's life expectancy. In these PLRs, the non-charitable beneficiaries did not have any condition that would be expected to result in a premature death, so their payment was calculated using their life expectancies, as determined by the IRS projections.

The above implies that if the non-charitable beneficiary has a shortened life expectancy, then he or she will receive less from the termination of the charitable remainder trust.

Early termination of a charitable remainder trust is usually accomplished through a court proceeding. The court proceeding will lead to additional costs for the non-charitable beneficiary and will result in less funds ultimately going to the non-charitable beneficiary.

The non-charitable beneficiary may receive 20% to 30% more in value if the income interest is sold rather than engaging in an early termination. There are companies that specialize in introducing purchasers of the non-charitable interests with those who hold an income interest in a charitable remainder trust. The purchasers are usually individuals and entities that have large tax deductions from net operating losses or operational losses to offset the income from the charitable remainder trust payments. One issue to consider is whether an income interest in the trust can be sold if the trust contains a spendthrift provision which might prevent alienation of any interest in the trust.

When selling the income interest in a charitable remainder trust, the selling party will recognize taxable gain, which should be considered before terminating a charitable remainder trust early. Additionally, if a broker is used, there will be a fee for the broker's services. It is important to understand how the broker's fee will be calculated and what services the broker will provide.

4. CLATs Must Pay Income Taxes on Receipt of IRA/Plan Proceeds. Because IRA/Plan benefits payable to a charitable lead annuity trust ("CLAT") will trigger income tax, a CLAT is typically not a good vehicle for charitable planning with IRA/Plans, but nevertheless may be an appropriate mechanism for passing after tax wealth to future generations for an estate taxable client. A "zeroed out" CLAT will qualify for a full estate tax charitable deduction by making sure that the net present value of all payments to be made to charity will equal the initial value of the CLAT's assets, but the CLAT will have to pay income taxes on the IRD received from an annuity. Thus, CLATs are not generally good candidates to receive IRA/Plan assets.

Below is a chart summarizing the various charitable options for planning with IRA/Plans:

CHARITABLE OPTIONS FOR PLANNING WITH IRA/PLANS

Type of Charitable Donation/Strategy	Private Foundation	Public Charity	Donor Advised Fund
Charitable Remainder Trust	Can be a beneficiary, but charitable deduction subject to Private Foundation AGI limitations if non-operating.	Yes, up to 50% of AGI deduction, 30% for capital gain property.	Same as listing a Public Charity as the charitable beneficiary (family can advise the Donor Advised Fund)
Qualified Charitable Donation (by taxpayer over 70½)	Not Allowed.	Up to $100,000 can be donated without the taxpayer paying any tax on the donation. Reduced for IRA contributions after age 70½	Not Allowed.
IRA Beneficiary Designation	Can be left to a Private Foundation on death for an estate tax charitable deduction.	Can be left to Public Charity on death of an estate tax charitable deduction.	Can be paid to Donor Advised Fund on death for estate tax charitable deduction.
Charitable Gift Annuity	Not per se prohibited but would likely be very difficult due to self-dealing rules and issues relating to the donor's retained control of the funds.	Yes. A deduction is allowed for the actuarial amount projected to go to charity.	Likely not allowed because the donor would have control of the funds. It may be possible if the Donor Advised Fund purchases a commercial annuity and keeps the difference.

CHAPTER 6 – CREDITOR PROTECTION PLANNING

Introduction

While most planners are aware of if and when the law in their applicable state will prevent normal creditors from being able to attach an IRA/Plan, a Surviving Spouse's rollover IRA, or an inherited IRA, planners need to also think through the creditor protection aspects associated with various payout arrangements, and how to protect from "Super Creditors" and "Exception Creditors" as discussed below.

For example, in most states, a rollover IRA owned by a Surviving Spouse will be exempt from the Surviving Spouse's creditors, but the Surviving Spouse who is the beneficiary of a Conduit Trust will lose Required Minimum Distributions to his or her creditors, even if the payments occur after he or she files a Chapter 7 bankruptcy.

The general federal law in this area is that IRA/Plans that are properly formed, funded and managed will be protected from creditors in bankruptcy, except to the extent that an IRA, based upon annual contributory IRA amounts, exceeds $1,362.800.[102] This is one good reason that normal annual contributory IRAs should be kept separate from IRAs rolled over from a deceased spouse or pension account.

Qualified Retirement Plans which are sponsored by an employer are generally protected from creditors both before and after the bankruptcy of the Plan Participant, because they are required by the federal employment law to have "spendthrift provisions" that prevent the Plan Participant from allowing a creditor to have a lien against the Plan or to reach the Plan balances.

In the U.S. Supreme Court case of *Clark v. Rameker*,[103] it was decided that the Bankruptcy Code does not protect an IRA that is inherited by a non-spouse, because the court did not consider inherited IRAs to meet the definition of "retirement funds" under Bankruptcy Code Section 522(b)(3)(C).

This decision leaves open the question as to whether a rollover IRA owned by a Surviving Spouse will be protected in bankruptcy, but most experts believe that such protection will apply because the rollover IRA is treated as the Surviving Spouse's own IRA for all purposes under federal tax law.

Many states provide creditor protection for IRAs in unlimited amounts and allow for that protection to apply in bankruptcy. For this reason, someone who resides in a state that does not provide such full protection, such as California, Minnesota, Maine or Hawaii, may want to move

[102] This amount is adjusted for inflation every third year on April 1. The next adjustment will be April 1, 2022.
[103] *Clark v. Rameker*, 573 U.S. 122 (2014).

to a state like Florida, which has an unlimited homestead exemption, more than 730 days before filing bankruptcy, in order to have the law of the destination state apply.[104]

Another form of creditor protection for IRAs and pension accounts involves having the IRA custodian invest in a limited liability company or other entity that can be disregarded for income tax purposes, but may deposit its assets into an account, or have them held by an LLC Manager sitused in a jurisdiction that will not permit creditors to reach the applicable assets.

This technique is the subject of an interview with Howard Rosen, Esquire, who is a well-known authority on creditor protection techniques and this strategy. A copy of this video can be received by emailing agassman@gassmanpa.com.

Further information on this topic can be found at Howard's excellent website, protectyou.com, or Howard can be contacted at bizz@protectyou.com.

The authors have not looked into whether such an arrangement could have a detrimental impact upon tax qualification of an IRA, but view this to be a legitimate planning option that can be considered for high risk IRA owners.

Some states provide protection for the owner or recipient of an annuity contract or payment. Planners can consider providing Charitable Remainder Annuity Trusts, Charitable Gift Annuities or simply having a beneficiary annuitize an IRA in order to have deferral of income tax and creditor protection planning, as further discussed in other chapters of this Book.

The following charts describe the various primary choices that Plan Participant and survivors have with respect to planning for IRA/Plans after the SECURE Act, and the creditor protection aspects thereof. Further discussion of this follows the charts.

SPOUSAL BENEFICIARY ARRANGEMENTS FROM A CREDITOR PROTECTION STANDPOINT

Method of Distribution	Payout/Taxation	Protection Under the Best State Laws*	Less Protective States	In Bankruptcy* (Assuming no state law protection)
Outright rollover	Best – deferred – slowest payout	Protected from creditors	Protected from creditors	Protected from creditors
Inherited IRA	Lifetime faster payout	Prortected from creditors	Not protected from creditors	Not protected from creditors

[104] Florida is usually the most popular state for individuals under these circumstances, because the Florida Supreme Court has ruled that the transfer of assets into a qualified homestead for the express purpose of avoiding a creditor cannot be set aside under the Florida Fraudulent Transfer Statute, and this will not be changed if and when Florida adopts the Uniform Voidable Transfers Act. Nevertheless, the Bankruptcy Code has provisions that will allow the court to set aside a fraudulent transfer into homestead that is made within ten years before the filing of a bankruptcy. Additionally, the Bankruptcy Code also disallows an individual from being entitled to the full homestead protection afforded by a particular state (such as Florida) unless the individual has owned the homestead property for at least the 1,215 days prior to filing bankruptcy. Moving to Florida may be considered to be a "fraudulent transfer."

Method of Distribution	Payout/Taxation	Protection Under the Best State Laws*	Less Protective States	In Bankruptcy* (Assuming no state law protection)
Conduit Trust (Spouse receives all withdrawals)	Lifetime faster payout	Payments not protected	Not protected from creditors	Payments not protected
Accumulation Trust (Trustee can accumulate distributions)	10-Year Rule applies	Payments well protected	Payments not protected	Payments not protected
Charitable Remainder Unitrust (Life or 20 years)	Stretches over years of payment	Payments not protected	Payments not protected	Payments not protected
Charitable Remainder Annuity Trust	Stretches over years of payment	Annuity payments may be protected (Florida – *In re Mart*)	Payments not protected	Payment not protected
Annuitized Annuity	Stretches over life of Surviving Spouse	Payments may be protected	Protected from creditor	Payments not protected from creditors

Note: Many states provide exemptions that will be respected in bankruptcy, based upon whether the state elected to opt in/opt out – Bankruptcy Code nevertheless will protect an individually owned IRA to the extent funded from a rollover from a Plan, plus up to $1,362,800[1] in value attributable to conventional IRA contributions and growth thereon.

NOTE: Only Accumulation Trusts funded after the death of the Plan Participant will be completely protected from Super Creditors – the IRS, the FTC, the SEC, criminal rstitution and some Medicare responsibilities. Only Accumulation Trusts may be protected from Exception Creditors (spouses, ex-spouses, child support, divorce attorney's fees and legal and associated costs incurred by a beneficiary who is not able to pay them), depending upon state law (Nevada and South Dakoa do not allow Exception Creditors to reach into an asset protection trust).

[1] This value is adjusted every three years for inflation, with the last increase occurring April 1, 2019.

NON-SURVIVING SPOUSE BENEFICIARY

Method of Distribution	Payout/Taxation	Protection Under the Best State Laws*	Less Protective States*	In Bankruptcy*
Inherited IRA	10 Years	Protected from creditors	Not Protected from creditors	Not Protected from Creditors
Conduit IRA (For minor child or older beneficiary) (not more than 10 years)	Lifetime	Payments Not Protected	Payments Not Protected	Not Protected from creditors
Accumulation Trust (Life Expectancy for disabled or	10 Years	Protected from Creditors	Protected from creditors	Not Protected from creditors

Method of Distribution	Payout/Taxation	Protection Under the Best State Laws*	Less Protective States*	In Bankruptcy*
chronically ill beneficiary – 10-Year Rule for anyone else)				
Charitable Remainder Unitrust	20 Years or Life Expectancy	Payments Not Protected	Not Protected from creditors	Not Protected from creditors
Charitable Remainder Annuity Trust	20 Years or Life Expectancy	Annuity payments may be protected (Florida – *In re Mart*)	Not Protected from creditors	Not Protected from creditors

*Debtors residing in many states will be able to use the better of the state law or the bankruptcy law upon filing bankruptcy.

Note: Many states provide exemptions that will be respected in bankruptcy, based upon whether the state elected to opt in/opt out – Bankruptcy Code nevertheless will protect an individually owned IRA to the extent funded from a rollover from a Plan, plus up to $1,362,800[1] in value attributable to conventional IRA contributions and growth thereon.

NOTE: Only Accumulation Trusts funded after the death of the Plan Participant will be completely protected from Super Creditors – the IRS, the FTC, the SEC, criminal rstitution and some Medicare responsibilities. Only Accumulation Trusts may be protected from Exception Creditors (spouses, ex-spouses, child support, divorce attorney's fees and legal and associated costs incurred by a beneficiary who is not able to pay them), depending upon state law (Nevada and South Dakota do not allow Exception Creditors to reach into an asset protection trust).

[1] This value is adjusted every three years for inflation, with the last increase occurring April 1, 2019.

CHOICES FOR MINOR IRA OR PENSION BENEFICIARY

"Don't handicap your children by making their lives easy."
– Robert A. Heinlein

	Payout Method to Apply	Advantages	Disadvantages[105]
1. Outright to Child	Over life expectancy, until child reaches age of majority – then 10-Year Rule applies – measured fromage of majority, as determined under state law	Simple, but may require appointment of guardian.	May result in loss, based upon poor judgment, creditor access,eventual divorce, etc.
2. To Custodian under Uniform Gift to Minors Act, or Equivalent State Law	Tax treatment same as #1 above.	The IRA/Plan and funds will be protected from indiscretion of the child until reaching the age that the child can take the arrangement over.	The child can take the arrangement over at a relatively young age (often 25), and creditorsof the child,divorcing spouses, etc., can reach the accounts atall ages.

[105] This Chart is also included in this Book on page 206.

	Payout Method to Apply	Advantages	Disadvantages[105]
3. Conduit Trust	Tax treatment same as #1 above. Could be payableto a Custodian of a Uniform Transfers to Minors Act account for a minor beneficiary.	Protects the principal of the IRA/Plan from indiscretion and creditors until 10 years after the child reaches age 21.	Expense of administering Conduit Trust, and requirement that all Required Minimum Distributions must be paid to child or Custodian (based upon life expectancy until reaching age of majority, and then everything mustbe paid out approximately 10 years after the child reaches age 21).
4. Accumulation Trust	10-Year Rule will apply – shortest payout of all alternatives.	Trustee can completely control if and when there will be withdrawals from the IRA/Plan, and if and when there will bedistributions to the child, if any.	Shorter payout, and expenses of operating Accumulation Trust.
5. TEA POT Trust – For Minor Beneficiary and Other Beneficiaries	Same as for #4 above.	Trustee can decide if and when the minor or other beneficiaries are mostdeserving, in need, or at lowest tax brackets.	Trustee discretion may disappoint the beneficiary – best to have a separate Equalization Trust and responsible Trustees.

SPECIAL BENEFICIARY ARRANGEMENTS FROM A CREDITOR PROTECTION STANDPOINT

Method of Distribution	Payout/Taxation	Protection Under the Best State Laws*	Less Protective States*	In Bankruptcy*
Payment to an Accumulation Trust for Disabled or Chronically Ill Beneficiary	Life Expectancy	Protected from Creditors	Protected from Creditors – May disqualify from some forms of public aid	Protected as a legitimate Third-Party Spendthrift Trust, if properly drafted
Conduit Trust for Not More than 10 Years Older Beneficiary	Life Expectancy	Payments Not Protected	Payments Not Protected	Not Protected
Accumulation Trust for Beneficiary Not More than 10 Years Younger	10-Year Rule	Payments Well Protected	Payments Well Protected	Protected from Creditors

*Debtors residing in many states will be able to use the better of the state law or the bankruptcy law upon filing bankruptcy.

NOTE: Only Accumulation Trusts will be completely protected from Super Creditors – the IRS, the FTC, the SEC, criminal restitution and some Medicare responsibilities. Only Accumulation Trusts may be protected from Exception Creditors (spouses, ex-spouses, child support, divorce attorney's fees and legal and associated costs incurred by a beneficiary who is not able to pay them), depending upon state law (Nevada, South Dakota, and certain other states do not allow Exception Creditors to reach into an asset protection trust).

1. What About Super and Exception Creditors?

Notwithstanding the state exemption statutes, Exception Creditors (such as divorcing and ex-spouses, children under child support statutes and lawyers and other professionals who represent the beneficiary of a trust who cannot afford to pay them), and also the "Super Creditor" agencies of the U.S. Government that are not prevented from seizing IRA/Plans under federal law must be considered. The agencies of the U.S. Government that have such Super Creditor rights include the Securities Exchange Commission, the Federal Trade Commission, the Internal Revenue Service, Medicare and other federal agencies for penalties, the Department of Justice for restitution, and the Federal Deposit Insurance Company in some circumstances. Making transfers for the purpose of avoiding the payment of amounts owed to such agencies will often be a criminal offense. *See Gassman & Markham on Florida and Federal Asset Protection Law*, Chapter 1, for more information on fraudulent transfers.

2. Accumulation Trusts

Contrary to what can occur to an individual who inherits an IRA/Plan or has one or more categories of the Exception Creditors or Super Creditors described above, IRA/Plans which are payable to an irrevocable trust that is established and funded by someone other than the beneficiary will not be reachable by normal creditors, Exception Creditors, or Super Creditors, when the trust is funded by someone other than the beneficiary, if properly drafted and managed.

It is strongly recommended that such trusts have clear language that enables an independent trustee to restrict and deny making any payments or providing any benefits to a beneficiary who may have a creditor situation, and that the beneficiary's rights over the trust be carefully limited.

This should not prevent the beneficiary from having the ability to replace the acting trustee or trustees with an independent trustee, or from requiring that the trust assets be properly invested and administered. It should also not prevent the beneficiary from being able to direct that trust assets may be paid to individuals or entities other than the individual, his or her estate, his or her creditors, or the creditors of his or her estate via the exercise of a properly drafted and limited power of appointment.

Trusts that are the beneficiaries of IRA/Plans that arose by reason of the death of Plan Participants occurring before 2020 can qualify for life expectancy payouts over the lifetime of an individual beneficiary of the trust, if the "See-Through Trust" requirements described in Chapter 4 have been met.

Such trusts can serve as excellent creditor protection vehicles.

3. Accumulation Trusts for Disabled and Chronically Ill Beneficiaries

The SECURE Act provides that only kind of Accumulation Trust that can accommodate receiving payments over the life expectancy of a beneficiary will be for an individual who is disabled or chronically ill under the definitions described in Chapter 2, Section 11 as of the date of the death of the Plan Participant.

All other properly drafted and funded Accumulation Trusts will be required to make withdrawals of all plan assets under the 10-Year Rule.

Accumulation Trusts established for disabled or chronically ill beneficiaries in certain states may disqualify those beneficiaries from receiving certain benefits or participating in certain programs, notwithstanding that such trusts will not cause disqualification from Medicaid or certain other programs in the vast majority of states. It is therefore important to consider whether a disabled or chronically ill individual might be best served by not having the provisions that are required to be incorporated to allow for a lifetime payment to apply, or to assure that the trust has the necessary "special needs trust" provisions in order to prevent such disqualification.

For this reason, we recommend that Trust Protectors be appointed with the ability to amend such a trust on or before the September 30th following the year of death of the Plan Participant, and also thereafter, in case it is in the better interests of the disabled or chronically ill individual or other family members to have such benefits held under a trust not dedicated solely to such individual, or possibly not having such individual as a beneficiary whatsoever.

4. Conduit Trusts

A Conduit Trust is a trust that is required to pay any amounts received from IRA/Plan withdrawals to the named beneficiary, in order to receive an advantageous payout arrangement.

Taxpayers must carefully balance the need for creditor protection against the utility of leaving assets in a Conduit Trust that can provide a more advantageous payout under the Life Expectancy Rule, and thus better deferral than under the 10-Year Rule. Because a Conduit Trust requires that all IRA/Plan distributions must be paid to the applicable individual beneficiary, such distributions will likely be subject to seizure by the judgement creditors of the beneficiary. Nevertheless, a Conduit Trust that requires the payment of all IRA/Plan distributions to the following categories of beneficiaries will cause the IRA/Plan to qualify for the Life Expectancy Rule so that Required Minimum Distributions can be paid over the beneficiary's life expectancy:

A. *The Plan Participant's Surviving Spouse*. While the IRA/Plan assets will be protected from creditors, all amounts withdrawn from the IRA/Plan must be paid to the Surviving Spouse and will therefore be accessible to his or her creditors, unless state law has a unique provision that would prevent this.[106]

B. *Older Beneficiary*. A beneficiary who is not more than 10 years younger than the deceased Plan Participant at the date of death of the deceased Plan Participant. As with a Surviving Spouse, all amounts withdrawn from the IRA/Plan must be paid to the applicable beneficiary. The Conduit Trust will protect what is left in the IRA/Plan on the death of such lifetime beneficiary, but Required Minimum

[106] As discussed in footnote 84, it is remotely possible that Florida law will not enable a creditor to reach amounts paid from an IRA or pension plan that have come through a Conduit Trust. See *In re Ladd* and *Gassman & Markham On Florida & Federal Asset Protection Law,* Chapter 8, Section C.

Distributions and any other payments from the IRA/Plan (which are required to be made) may be attached by creditors, even after the beneficiary has filed bankruptcy.

C. *Minor Child of Plan Participant*. A minor child of the Participant (but not any other descendants) where the Conduit Trust requires life expectancy payments until the child reaches age 21, after which the 10-Year Rule applies. This will only protect the principal of the IRA/Plan that remains in the Conduit Trust until the principal has to be paid out in the 11th year after the child reaches age 21, meaning that a great many creditors of 28-year-olds will celebrate that particular birthday.

When clients have large IRA/Plans that may benefit a minor child, they may be best advised to have a portion of those accounts go into Conduit Trusts that will be expected to be fully spent on the child before he or she reaches the 10th anniversary date of the age of majority, with the remaining amounts going to Accumulation Trusts, or a “TEA POT” Trust System to allow the income to be sprayed out over the 11 years in the most efficient manner possible, and then held, net of taxes, after the 11th year, in a creditor protected manner, as opposed to having to be paid out of the trust when the proceeds of the IRA account must be paid out to the trustee from the Accumulation Trust after the 11th year. Discussion of the “TEA POT Trust” planning arrangement can be found in Chapter 7.

D. *Disabled or Chronically Ill Participant*. An Accumulation Trust can be used for a disabled or chronically ill beneficiary, as described in Section 3 above.

One question is what would happen if a Conduit Trust has provisions that enable Trust Protectors to modify the trust or decant it into a different trust in the future that would not require a full payout upon reaching age 21. Would the presence of such flexibility cause the loss of Conduit Trust status? Planners may wish to carefully review decanting and similar statutes and laws in order to determine whether a Conduit Trust may be decanted or otherwise modified for creditor protection purposes, and what impact this may have upon allowing the trust to qualify for “See-Through” status.

Because we cannot predict what eligibility rules may apply in the future, it seems prudent to at all times have Trust Protectors or other fiduciaries or mechanisms which will permit such a trust to be modified, but it is unknown whether such flexibility could cause such a trust to not qualify for lifetime payout purposes by reason of not being considered to have met the requirement that the trust was irrevocable on the date of the Plan Participant’s death, or was intended to change after a number of years from a trust that would qualify as a Conduit Trust to a trust that would not qualify if the Trust Protectors chose the trust language to prevent a full payout once the Trustee is required to take a distribution of all remaining trust assets when required under the 10-Year Rule.

5. Marital Agreements to Protect Roll Over or Inherited IRAs

While the rollover IRA gives the most flexibility and income tax deferral for a Surviving Spouse, it also exposes the rollover IRA and distributions therefrom to possible loss from poor investment practices, overspending, or being payable to an undesired beneficiary if the Surviving Spouse leaves the IRA/Plan or assets received from the IRA/Plan to beneficiaries not selected or approved by the first dying spouse.

Some clients may wish to receive this optimum tax treatment instead of more protective but less tax effective conduit or Accumulation Trusts by entering into Marital Asset Protection System ("MAPS") Agreements that contractually bind the Surviving Spouse to invest conservatively, or based upon the advice of a named fiduciary or a trust company that may be selected and replaceable by the Surviving Spouse, to withdraw no more than the Required Minimum Distributions, and to spend no more than is reasonably necessary, while saving amounts distributed and taking steps to assure that the remaining IRA assets and amounts from distributions that were reinvested will pass based upon the terms of the applicable agreement.

It is unknown whether such an agreement may be considered to be a "constructive trust" that would cause the 5-Year Rule or 10-Year Rule to apply. Thus, the MAPS Agreement should include language that prevents the remedy of constructive trust from applying and provides that the cause of action held by third-party beneficiaries, which may include the descendants or a trust for the descendants of the first dying spouse to be limited to causes of action other than having a constructive trust or allowing the third-party beneficiaries to have equitable claims to the rollover IRA.

In addition, or alternatively, a Credit Shelter and/or QTIP Trust arrangement left for the Surviving Spouse to hold other assets may require that the conduct of the rollover IRA must be compliant with the requirements set forth above, in order for the Surviving Spouse to receive any distributions, and to have any rights over the Credit Shelter Trust, or to receive anything other than the minimum required income, which must be distributed under the QTIP Trust.

Such an agreement could also provide that a fiduciary (who may not be favored by the Surviving Spouse) to serve as sole trustee of any such trusts, if and when the Surviving Spouse has not complied with all required terms with respect to management of the rollover or inherited IRA/Plan.

6. Inherited IRA or Annuitization to Avoid the 10% Excise Tax for Withdrawals before age 59½

When the Surviving Spouse is under age 59½, and expects to need to take withdrawals from the IRA before then, the Spouse may be well advised to treat a portion of the IRA/Plan as an inherited IRA or should consider annuitizing such portion in order to be able to receive distributions before age 59½ without triggering the 10% excise tax under Internal Revenue Code Section 72(t). There are a number of exceptions to the early withdrawal penalties, which include, under certain circumstances, large medical bills, first-home purchases, disability, and expenses for higher education. Additionally, as a result of the CARES Act, an exception applies for a Coronavirus-Related Distribution, as described in Chapters 1 and 2 of this Book.

CHAPTER 7 – THE SECURE ACT

The SECURE Act of 2019 is one of the most dramatic and widespread changes in income tax/estate planning law that the authors have seen in many years.

This Act will immediately impact thousands of taxpayers, and thousands of documents and beneficiary designation arrangements now in place will do significant harm, for the reasons described in this Chapter.

It is essential that estate planners and tax advisors reach out to clients to inform them of the need for change in many situations.

The good news is that, in most situations, the choices are much easier to understand than many of the alternatives that had to be considered in the past, and that in any given situation there are usually only four choices, and fairly obvious primary criteria for making a decision.

It is therefore crucial that advisors understand how the SECURE Act will affect Retirement Plans, and, most importantly, what planning should be implemented to address the effects of the Act.

Readers who are not familiar with pension and IRA payout rules and trust planning associated therewith may wish to review Chapters 1 through 3 to have a general understanding of how the rules work, while permitting this Chapter to be the basic and "deep dive" discussion of the rules that apply where Plan Participants have died after 2019.

For many families with large IRA/Plan account balances, and other non-IRA/Plan assets who are facing 10-year payout situations under the 10-Year Rule, will instead use a "Two POT Trust" arrangement. Under this system, which we call the TEA POT Trust System℠ (the Tax Efficient Accumulation POT Trust System℠),[107] one POT Trust (known as the "TEA POT Trust") will receive the IRA/Plan after the death of the Participant. The IRA/Plan will be subject to the 10-Year Rule. The Trustee will have the power to sprinkle distributable net income among beneficiaries in the most tax efficient manner as and when distributions are received from the IRA/Plan by distributing income to beneficiaries in lower tax brackets or beneficiaries who have favorable tax attributes, such as net operating or suspended losses. The second POT Trust (known as the "Equalization Trust") will hold assets that do not generate significant levels of income, such as equities and municipal bond funds, and the trustee of the second POT Trust can make distributions to beneficiaries who are in higher tax brackets in order to make up for distributions made to other beneficiaries from the IRA/Plan POT Trust.

The use of a shadow trust to become the beneficiary of IRA/Plans after the death of the Plan Participant has been commonly used in the past as retirement plan trusts often require that specific rules and limitations be followed in order to qualify the trust as a "See-Through Trust," and may therefore provide sufficient justification to establish a multiple trust arrangement for reasons other

[107] The Twin TEA POT Trust System℠ is a Service Mark owned by Gassman, Crotty & Denicolo, P.A.

than to avoid income tax. The use of the TEA POT Trust System℠ is discussed in more detail below.

The More Things Change the More They Stay the Same

RECENT CHANGES IN TRUST LAWS [108]

ITEM	PRE-2020 LAW	POST-2019 LAW
Required Beginning Date	Upon the later of: (a) April 1 of the calendar year following the year in which the Participant attains the age of 70½; or (b) April 1 of the calendar year following the year in which the Participant retires from employment, but only if the Participant is not a 5% owner of the stock of the employer or stock possessing more than 5% of the total combined voting power of all stock of the employer who sponsors the plan.	The reference to age 70½ has changed to 72 so that the Required Beginning Date is now the later of: (a) April 1 of the calendar year following the year in which the Participant attains the age of 72; or (b) April 1 of the calendar year following the year in which the Participant retires from employment, but only If the Participant is not a 5% owner of the stock of the employer or stock possessing more than 5% of the total combined voting power of all stock of the employer who sponsors the plan.
Life Expectancy Rule / 10-Year Rule	An individual beneficiary, or a trust that qualifies as a Conduit Trust or an Accumulation Trust, which is a beneficiary of any IRA/Plan qualifies for the Life Expectancy Rule (assuming that the IRA/Plan does not preclude application of Life Expectancy Rule). The Life Expectancy Rule allows Required Minimum Distributions to be made from the IRA/Plan over the life expectancy of the beneficiary (or a beneficiary of the trust).	In lieu of Life Expectancy Rule, the 10-Year Rule will apply where the IRA/Plan is left to an individual or to a trust that qualifies as a Conduit Trust or an Accumulation Trust. The 10-Year Rule requires that all assets be distributed from the IRA/Plan no later than December 31st of the 10th calendar year after the Plan Participant's death, and, under the Proposed Regulations, also requires that the beneficiary of the IRA/Plan take Required Minimum Distributions in years 1-9 following the Plan Participant's death if the Plan Participant died on or after his or her Required Beginning Date. Exceptions to this include IRA/Plans that are made payable to Eligible Designated Beneficiaries, or to Conduit Trusts for the sole benefit of Eligible Designated Beneficiaries (defined below).
5-Year Rule /At-Least-As-Rapidly Rule	The default Required Minimum Distribution Payout Rule states that all assets must be distributed out of the IRA/Plan no later than December 31 of the year that is 5 years after the calendar year of the Plan Participant's death. An exception to this applies where the Plan Participant dies after reaching his or her Required Beginning Date, in which event the Required Minimum Distributions from the IRA/Plan can be paid over the life	This Rule has not changed.

[108] This table is also included in this Book at page 83.

ITEM	PRE-2020 LAW	POST-2019 LAW
	expectancy of the deceased Plan Participant based upon the deceased Plan Participant's age under the single life table, without annual recalculation of life expectancy.	
Conduit Trust	A trust that is required to pay all amounts withdrawn from an IRA/Plan immediately to a Designated Beneficiary was usually permitted to take distributions over lifetime of Designated Beneficiary.	Now defined under the Proposed Regulations as a See-Through Trust which provides that all distributions from the IRA /Plan will be paid to the or for the benefit of specified beneficiaries upon receipt by the trustee. The rules regarding qualification of a Conduit Trust continue to apply, but the 10-Year Rule will apply in lieu of the Life Expectancy Rule unless the Designated Beneficiary of the Conduit Trust is an Eligible Designated Beneficiary. Additionally, the law continues to treat the Designated Beneficiary of a Conduit Trust as if the Designated Beneficiary inherited the IRA/Plan directly.
Accumulation Trust	A trust that permits a Trustee to accumulate distributions from the IRA/Plan, and also qualifies to be considered as a "See-Through Trust" whereby the IRS will look to a beneficiary of the Trust as the Designated Beneficiary of the IRA/Plan for the purposes of determining the Required Minimum Distribution payout. Would usually be treated the same as a Conduit Trust to allow lifetime annual distributions, not annually recalculated.	Now defined under the Proposed Regulations as a See-Through Trust that is not a Conduit Trust. The rule regarding qualification of an Accumulation Trust continue to apply, but the 10-Year Rule will apply in lieu of the Life Expectancy Rule unless the sole lifetime beneficiary of the Trust is a chronically ill or disabled Eligible Designated Beneficiary, or in certain limited circumstances where an Accumulation Trust benefits only Eligible Designated Beneficiaries during their lifetimes. Nevertheless, an Accumulation Trust can be used to have the 10-Year Rule apply instead of the 5-Year Rule or At-Least-As-Rapidly Rule (the Ghost Life Expectancy Rule).
Inherited IRA	After IRA/Plan Participant dies, beneficiary maintains the IRA and it is designated as an "Inherited IRA," then Life Expectancy Payout can apply without penalties for withdrawal if beneficiary is under 59½, but lifetime distributions must begin in the year after the year of death of the Participant (unless the Surviving Spouse is the sole beneficiary, in which event the distributions can be postponed until the spouse reaches his or her Required Beginning Date).	Same Rule applies, except that the Life Expectancy Rule is available only if an Eligible Designated Beneficiary is the sole beneficiary of the inherited IRA. If an Eligible Designated Beneficiary is not the sole beneficiary of the Inherited IRA, then the 10-Year Rule applies in lieu of the Life Expectancy Rule.

ITEM	PRE-2020 LAW	POST-2019 LAW
Eligible Designated Beneficiaries (EDBs)	Did not exist under prior law.	Certain beneficiaries are afforded the ability to have a Life Expectancy Rule apply in lieu of the 10-Year Rule. There are five beneficiaries who are considered as Eligible Designated Beneficiaries, but they have varying rights which are briefly summarized as follows: (1) Surviving Spouse – may roll over or use Inherited IRA and withdraw over Life Expectancy, with annual recalculation, as under past law. May be inherited outright to child or under Conduit Trust to have the above deferral. (2) Minor Child of Deceased Plan Participant (but not a minor grandchild or any other minor), if inherits from Inherited IRA of Surviving Spouse, 10-Year Rule applies. If a minor child inherits from IRA or Rollover IRA of either parent, then withdrawal each year based on Life Expectancy until Age of Majority, then 10-Year Rule applies. May be inherited outright to child or under Conduit Trust to have the above deferral. (3) Disabled Beneficiaries – may use Life Expectancy Rule if IRA/Plan is left to such beneficiary directly, to a Conduit Trust for the beneficiary's benefit, or to an Accumulation Trust for the beneficiary's sole benefit. If the IRA/Plan is left to an Accumulation Trust that is not for the sole benefit of such beneficiary, then the 10-Year Rule applies. (4) Chronically ill individuals – Same as Disabled Beneficiaries above. (5) Beneficiary Less Than 10 Years Younger Than Plan Participant – May use Life Expectancy if IRA/Plan is payable directly to such beneficiary or to a Conduit Trust for such beneficiary. The 10-Year Rule applies if the IRA/Plan is left to an Accumulation Trust. NOTE: If the Plan Participant dies after reaching his or her Required Beginning Date, then any beneficiary can use the At-Least-As-Rapidly Rule to choose to withdraw Required Minimum Distribution over the life expectancy of the deceased Plan Participant based upon his or her life expectancy under the single life table, without annual recalculation.

ITEM	PRE-2020 LAW	POST-2019 LAW

Before working methodically through the new rules and situations to which they apply, it will be useful for some readers understand the primary rules that will continue to apply:

1. When an IRA/Plan is made payable directly to an individual beneficiary who was married to the Plan Participant, the Surviving Spouse can roll the IRA/Plan into his or her own "Rollover IRA" and treat the IRA as if it was his or hers from the beginning.

   Alternatively, if the Surviving Spouse wants to take out distributions before age 59½ and avoid the 10% excise tax on distributions taken by a Participant before he or she reaches age 59½ (that would not apply if the Surviving Spouse rolls over the IRA/Plan into his or her own IRA), he or she can treat all or part of IRA/Plan as an Inherited IRA and begin to take distributions each year that are equal to or greater than the Required Minimum Distribution amounts based upon the Surviving Spouse's life expectancy. Under this approach, the Surviving Spouse can take Required Minimum Distributions from the Inherited IRA over his or her life expectancy under the Single Life Table, with annual recalculation.

2. A Plan Participant who reached the age of 70½ in 2019 was required to distribute the first Required Minimum Distribution by April 1, 2020 to avoid penalties. A Plan Participant who had not yet reached age 70½ in 2019 will not have to take a Required Minimum Distribution until April 1st of the calendar year following the calendar year in which the Plan Participant reaches the age of 72.

   It is noteworthy that the failure to make an annual Required Minimum Distribution without good cause will result in a penalty equal to 50% of the amount of the Required Minimum Distribution which has not been made.

3. Individuals who have reached age 70½ can cause distributions of up to $100,000 a year to pass directly to charity to have the equivalent of a 100% charitable deduction by making a Qualified Charitable Distribution (QCD) from the IRA/Plan directly to public charity as described in Chapter 5. This opportunity becomes available when an individual attains the age 70½, notwithstanding that Required Minimum Distributions do not begin until after the Plan Participant reaches age 72.

4. The Pre-SECURE Act law applies to any IRA/Plan where the Plan Participant has died prior to January 1, 2020, and the SECURE Act applies to beneficiaries who inherit an inherited IRA when the lifetime beneficiary has died on or after January 1, 2020.

   A spouse who would have otherwise inherited an IRA/Plan from a Plan Participant who died in 2019 can make a disclaimer within 9 months of the date of death of the Plan Participant, and therefore have the IRA/Plan assets pass to or for the benefit of descendants or other contingent beneficiaries under the prior rules which allow for the beneficiaries to potentially "stretch" the IRA/Plan Required Minimum Distributions over the life expectancy of the beneficiary.

This made a significant difference as to whether the Surviving Spouse of a Plan Participant who has before January 1, 2020 elected to roll over an inherited IRA/Plan, to accept the benefits of a Conduit Trust or Accumulation Trust, or to disclaim whatever interest the Surviving Spouse would have had to enable descendants or other individual beneficiaries to use their entire life expectancy for distributions.

Further, the 2022 Proposed Regulations confirm that the death of a Designated Beneficiary who has been receiving Required Minimum Distributions over his or her life expectancy following the death of a Plan Participant who died before January 1, 2020, will cause the SECURE Act rules to apply.

If a Plan Participant who died before January 1, 2020 left an IRA/Plan to a trust that has more than one Designated Beneficiary (such as an Accumulation Trust with multiple individual beneficiaries), then the SECURE Act will apply upon the death of the oldest trust beneficiary, if the trust beneficiary dies on or after January 1, 2020.

5. The Life Expectancy Rule has largely been eliminated for most non-spouse beneficiary situations, and in most situations replaced with the 10-Year Rule whereby all assets must be distributed from the IRA/Plan by December 31st of the 10th year following the calendar year of the Plan Participant's death. An exception allows the Life Expectancy Rule to continue to apply where the IRA/Plan is payable directly to an Eligible Designated Beneficiary to a Conduit Trust that is required to distribute all IRA/Plan withdrawals to an Eligible Designated Beneficiary.

   The term Eligible Designated Beneficiary means any person who is in one of the following categories, as also described in Chapter 2, Section 11:

   (1) the Plan Participant's Surviving Spouse;

   (2) a disabled beneficiary;

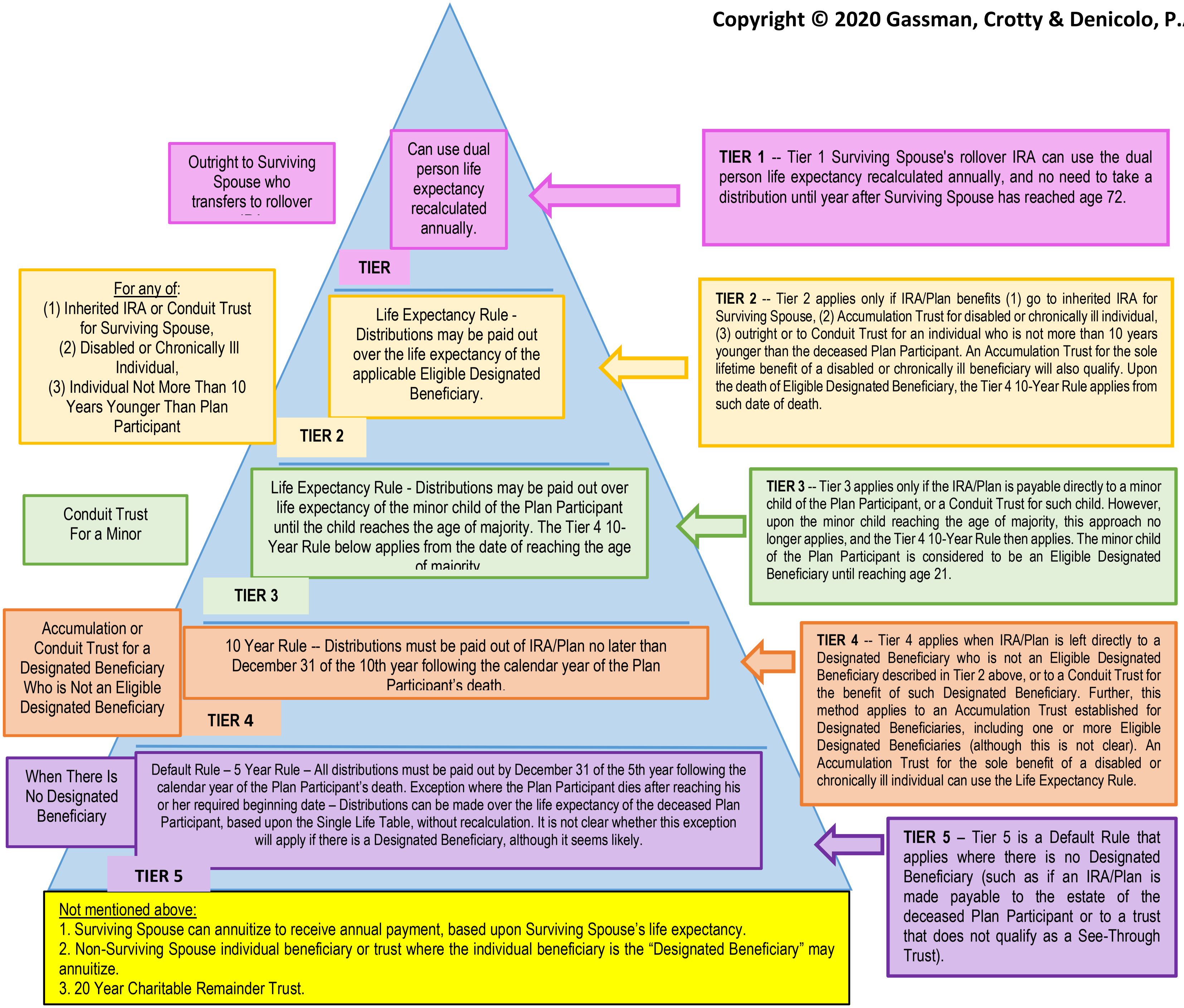
   (3) a chronically ill beneficiary;

   (4) a beneficiary who is no more than 10 years younger than the Plan Participant; or

   (5) a minor child (but only until the minor child reaches the age of "majority," as determined under state law, in which case the 10-Year Rule will apply to require that all assets must be distributed from the IRA/Plan by December 31st of the 10th year following the calendar year of the child reaching age 21).

The following "Pyramid" Chart describes the Required Minimum Distribution tiers as a result of the new rules provided under the SECURE Act:

REQUIRED MINIMUM DISTRIBUTION TIERS UNDER THE SECURE ACT



6. The advantages of income tax deferral for older individual beneficiaries are often overstated, but, relative to the ability to stretch Required Minimum Distributions over the beneficiary's life expectancy based upon the Life Expectancy Rule, the 10-Year Rule can make a big difference from a mathematical standpoint.

While it is usually advantageous to defer income taxes from an income tax planning standpoint, the difference in terms of the actual after-tax net value of applicable assets available for intended beneficiaries should be reviewed on spreadsheets to be understood.

Under the previous law, IRA/Plans that were inherited by individuals or properly drafted See-Through Trusts for individuals could be paid out over the life expectancy of the individual (in the case of an individual being the direct beneficiary of the IRA/Plan), or over the life expectancy of the oldest beneficiary of the trust who could receive benefits from IRA/Plan (in the case where the trust is a beneficiary). An IRA/Plan that can be paid out over the life expectancy of a beneficiary is known as a "Stretch IRA." However, for most non-spouse beneficiaries, and for Accumulation Trusts held for a Surviving Spouse, the lifetime Stretch IRA has been eliminated. The effects of this change are drastic.

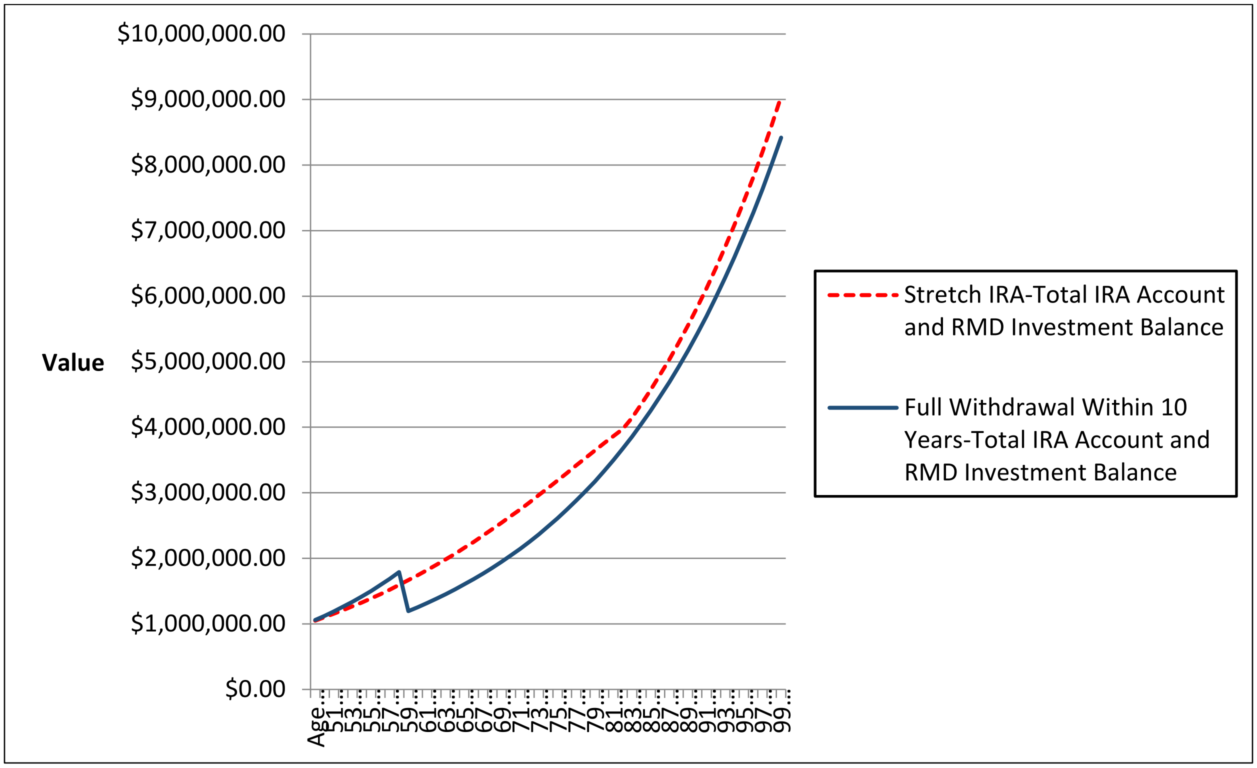
The growth in value inside an IRA/Plan over a number of years will cause a significant advantage for a lifetime payout beneficiary that simply is not available under the SECURE Act.

The authors have run calculations to determine the impact of the 10-Year Rule, as opposed to deferral over a Designated Beneficiary's life expectancy, and the long-term impact is substantial. For example, assuming that a 50-year-old non-spouse beneficiary is the Designated Beneficiary of a $1,000,000 IRA that will have assets that grow at a 6% annual rate of return, and that the beneficiary is in the 37% income tax bracket, and will reinvest amounts distributed at a 5% after-tax rate of return, the loss of life expectancy deferral will result in a $470,492 difference in the amount of total assets remaining after taxes 10 years after the death of the Plan Participant, assuming that the 10-Year Rule applies. The difference is $594,905 after 20 years and $470,810 after 30 years. This is a very large difference.

Charts summarizing the numbers are as follows:[109]

[109] The numbers will be updated when the next edition of the book is released, which will be shortly after the Proposed Regulations are finalized.

LONG-TERM IMPACT OF 10-YEAR RULE OVER DESIGNATED BENEFICIARY'S LIFE EXPECTANCY



The differences are much less pronounced when a Surviving Spouse age 50 may choose between a rollover, a Conduit Trust or an Accumulation Trust, as pointed out in our LISI Estate Planning Newsletter #2387 (February 10, 2015) at http://www.leimbergservices.com, entitled "Ten Portability Mistakes and What You Need to Know to Avoid Them."

The same rules continue to apply when the spouse is the beneficiary of a Conduit Trust; however, if the spouse is a beneficiary of an Accumulation Trust, the 10-Year Rule will apply and result in a much less favorable Applicable Payout Mode than the Life Expectancy Rule.

The bottom line is that it will be better in most situations to require that distributions be held in trust when there is a significant risk that a Surviving Spouse or other beneficiary would "misdirect, mismanage, or over spend" an inherited IRA or retirement account. Sometimes, focusing on tax implications to the detriment of non-tax planning considerations, such as misuse or improper spending of assets, can be foolish.

7. Conduit Trusts and Accumulation Trusts are still permissible and viable under the new law, but their utility was limited under many circumstances.

Conduit Trusts and Accumulation Trusts are collectively known as "See-Through Trusts," and are special types of trusts whereby the IRS will look through the Trust to a Designated Beneficiary in order to determine whether the IRA benefits can be paid out over a period longer than 5 years or the life expectancy of the deceased Plan Participant, if the Plan Participant died after his or her Required Beginning Date. The SECURE Act retains the baseline default rule of the prior law which provides that the assets of any IRA/Plan that is paid to a non-individual or to a Trust that does not qualify as a See-Through Trust must be distributed within 5 years of December 31st of the calendar year of the Plan Participant's death, or the life expectancy of the deceased Plan Participant if the Plan Participant died after his or her Required Beginning Date (the "At-Least-As-Rapidly Rule").

To review the discussion of Chapter 3, in order to qualify as a See-Through Trust, a Trust must be a Conduit Trust or an Accumulation Trust meeting the following requirements:

(A) The trust must be an irrevocable trust, at least on the day of the Plan Participant's death, and must be valid under applicable state law.

(B) All beneficiaries of the trust are individuals and identifiable by the Designation Date (September 30th of the calendar year following the Plan Participant's death). It is acceptable for the trust to have only one beneficiary.

(C) Information regarding the trust must be provided to the plan administrator by October 31st of the calendar year following the Plan Participant's death.

(D) None of the trust assets can be available or used to pay creditors of the trust or the estate of the deceased Plan Participant after September 30th of the calendar year of the Plan Participant's death.

A Conduit Trust is easier to draft and administer than an Accumulation Trust because the only requirement (other than the above) is that any and all monies distributed from the IRA/Plan to the trust must be immediately distributed to one or more named beneficiaries, referred to as the Designated Beneficiary. The primary disadvantage of a Conduit Trust is that the Designated Beneficiary has to receive payment, even if there are creditors, a divorce or spendthrift issues.

An Accumulation Trust is a Trust which provides that the trustee can accumulate benefits for the benefit of one or more beneficiaries, so long as the Trust meets certain requirements, such as not having any non-individuals as beneficiaries of the Trust as of September 30th of the calendar year following the death of the Plan Participant, or any non-individuals as potential appointees under any power of appointment.

It is noteworthy that traditional provisions related to limiting the beneficiaries of such Trust to beneficiaries that are younger than the Designated Beneficiary are no longer applicable due to the fact that Accumulation Trusts are generally subject to the 10-Year Rule and not the Life Expectancy Rule. The lifetime stretch that these See-Through Trusts provided under the prior law has been replaced with a 10-Year Rule in most non-spousal situations, as further described below.

If and when an Accumulation Trust can receive distributions over the life expectancy of a named beneficiary, which would now only apply for a disabled or chronically ill beneficiary, the birth date of the oldest disabled or chronically ill beneficiary of the Trust will likely be controlling in the unlikely event that an Accumulation Trust would be payable to multiple disabled or chronically ill beneficiaries. In all other circumstances, the 10-Year Rule will apply when an Accumulation Trust is made the beneficiary of an IRA/Plan.

RULES THAT APPLY TO SEE-THROUGH TRUSTS

THE RULES THAT APPLY TO SEE-THROUGH TRUSTS		
Apply to Both Accumulation and Conduit Trusts	Apply Only to Accumulation Trusts	Apply Only to Conduit Trusts
Any Accumulation or Conduit Trust must meet the following requirements in order for the Stretch Rules to apply:		
A. The trust must be valid under state law.	A. Powers of Appointment Must be Limited Only to Certain Appointees	A. Distributions Must be Paid to the Trust Beneficiary Upon Receipt by the Trustee
B. The trust must be irrevocable, at least immediately after the death of the Plan Participant	B. If Accumulation Trust is for an Eligible Designated Beneficiary, then Permit Powers of Appointment Only in Favor of Individuals Who Are Younger Than the Eligible Designated Beneficiary.	B. Remainder Beneficiaries and Others Do Not Count for Required Minimum Distribution Purposes.
C. The beneficiaries of the trust must be identifiable by being named, or by being members of a class of beneficiaries that makes each person identifiable.	C. Contingent Beneficiaries Count for Required Minimum Distribution Purposes	C. Conduit Trust Can Pay Trust Expenses.
D. Only Beneficiaries on the Designation Date (September 30 of the year after the Plan Participant's death) count		
E. Information must be provided to the Plan Administrator by October 31 of the year after the year of the Plan Participant's death.		

8. Good News for Individuals Who Have Not Had to Begin Taking Annual Required Minimum Distributions, and Individuals over the Age of 70½ That Want to Continue Contributing to Traditional IRAs.

The Required Beginning Date of individuals who did not reach age 70½ by December 31, 2019 will be no earlier than age 72 under the SECURE Act. This gives such individuals an additional 1½ years to defer taking Required Minimum Distributions. The SECURE Act allows taxpayers with "earned income" to make contributions to traditional IRAs beyond the age of 70½. Previous law prohibited contributions to traditional IRAs upon an individual reaching the year in which they attain the age of 70½. Therefore, individuals who have earned income from wages or self-employment can make contributions to traditional IRAs in 2020 and each year thereafter, regardless of their age (so long as they have earned income).

A Plan Participant who has reached the Required Beginning Date can take some or all of the first year Required Minimum Distributions on any day or days during the calendar year in which the Required Beginning Date is reached, or by April 1st of the following calendar year.

9. Good News for Roth IRA and 401(k) Holders.

Roth IRA and Roth 401(k) Plans still pay out tax-free and follow the same Required Minimum Distribution rules that apply to taxable plans. The new rules continue to permit Roth IRA and Roth 401(k) holders to retain these accounts without taking any Required Minimum Distributions during the lifetime of the Plan Participant. The accounts continue to grow tax-free, and what is taken out of the account will also be tax-free.

The fact that many families will be taxed sooner and at higher income tax rates on inherited IRAs pushes the scale towards converting, regular 401(k)s and pension plans, and traditional IRAs, into Roth accounts. Nevertheless, clients should be cautious before paying income taxes now based upon the possibility of future income tax savings. As we have learned many times over, the tax law is permanent only until Congress decides to change it.

For example, taxpayers of moderate means might have a tremendous need for money from their IRA to pay for home health care expenses, and may have significant tax deductions that will offset the withdrawals from IRA/Plan when the home health care paid for has been prescribed by a physician. See Leimberg Employee Benefits and Retirement Planning Newsletter #549 by Alan Gassman, Kenneth Crotty and Christopher Denicolo entitled *One Good Reason Not to Do a Roth IRA Conversion*.

10. The Default 5-Year Rule and Designated Beneficiary Concept Are Still in Effect, Although the Life Expectancy Rule Has Been Replaced by the New 10-Year Rule (With Five Notable Exceptions).

Previous law provided that all assets held under an IRA/Plan must be distributed out of the plan within five years of December 31st of the calendar year of the Plan Participant's death, unless one of the following applied:

(a) The Plan Participant died before 2020, but after his or her Required Beginning Date, in which event the post-death Required Minimum Distribution payments could have been made over the life expectancy of the deceased Plan Participant as if he or she were still alive; or

(b) The assets in the IRA/Plan could have been distributed annually over the life expectancy of the Designated Beneficiary named by the deceased Plan Participant.

The ability to "stretch" Required Minimum Distributions from IRA/Plans over the life expectancy of a non-spouse beneficiary or the Plan Participant's life expectancy was the foundation for the pre-2020 "Stretch IRA" planning technique. This allowed for distributions from an inherited IRA/Plan and the corresponding income tax burden associated with such distributions, to be deferred over many years.

The primary change to the above under the SECURE Act is that the Life Expectancy Rule has been replaced by a 10th year payout deadline under the 10-Year Rule, with no annual distributions being required until December 31 of the 10th year, except in the case of Eligible Designated Beneficiaries in certain situations. Therefore, the Stretch IRA for many clients no longer applies, and instead all assets must be paid out from the IRA/Plan within 10 years of December 31st of the calendar year in which the Plan Participant dies.

While the 2022 Proposed Regulations discussed in detail in Chapter 8 are largely favorable to taxpayers, the biggest and most unpleasant surprise relates to Required Minimum Distributions following the death of a Plan Participant who dies after reaching his or her Required Beginning Date when the 10-Year Rule applies.

Specifically, the Proposed Regulations state that a beneficiary who inherits an IRA/Plan from such a Plan Participant after reaching his or her Required Beginning Date will be required to receive distributions beginning on the first calendar year following the year of the decedent's death, each year until the 10th year following the calendar year of the decedent's death when all assets in the IRA/Plan will have to be distributed outright to such beneficiary by December 31 of such 10th year.

This is a departure from the "10-Year Rule" under the statute as understood by many practitioners and commentators, where the beneficiaries of the deceased Plan Participant's Retirement Plan who are subject to the 10-Year Rule would not be required to receive any distributions following the death of the decedent until December 31 of the 10th year following the calendar year of the decedent's death (regardless of the decedent's age at death).

Many practitioners and commentators find this IRS interpretation to be shocking, as a parallel "5-Year Rule" has been in effect for decades, and such 5-Year Rule has never been interpreted or construed to require distributions to be made from the Retirement Plan before December 31 of the 5th year following the deceased Plan Participant's death.

Nevertheless, commentators have expressed concern that taxpayers and trusts may be severally penalized for failure to receive distributions under rules that are very difficult to understand. Given this situation, trustees of trusts may wish to err on the side of caution and receive Required Minimum Distributions during the initial ten years if doing so will not have a significant tax impact.

While the lifetime stretch IRA has been eliminated for most situations where the Surviving Spouse is not the sole beneficiary of the IRA/Plan, the concept of a Designated Beneficiary is still alive and well. As stated above, the Designated Beneficiary is an individual or individuals named as a beneficiary of the IRA/Plan. When a certain type of trust satisfies the IRS' rules to qualify as a See-Through Trust, the oldest trust beneficiary is considered to be the Designated Beneficiary. Before 2020, the Designated Beneficiary's life expectancy will be used to determine the distribution period for Required Minimum Distributions, and such distribution period would continue to apply even after the Designated Beneficiary has died. Now, the 10-Year Rule applies in most cases where the Life Expectancy Rule would have applied.

Therefore, trusts which will receive IRA/Plan benefits will still need to qualify as See-Through Trusts to have the benefit of the 10-Year Rule, and must have special provisions which will allow the trust to qualify as a See-Through Trust in order to be able to take advantage of the 10-Year Rule. If such a trust does not have the special provisions, then the 5-Year Rule will apply, unless the At-Least-As-Rapidly Rule applies because the Plan Participant died after his or her Required Beginning Date (after age 72). Accordingly, a trust must be specially designed to not benefit any charities or non-individual beneficiaries, and to meet the other requirements necessary to qualify a trust as a See-Through Trust; however the consequences for not properly qualifying as a See-Through Trust are not nearly as punitive as they have been in the past where the 10-Year Rule would now apply.

11. "Eligible Designated Beneficiaries" Are Excepted from the 10-Year Rule, and Are Entitled to Use the Life Expectancy Rule (Although Temporarily in Some Cases)

Under the new rules, a payout over the life expectancy of a Designated Beneficiary can only apply in the below enumerated circumstances which apply only when IRA plans are made payable to or for the benefit of certain beneficiaries known as the "Eligible Designated Beneficiaries." In the case of such Eligible Designated Beneficiaries, the Life Expectancy Rule can allow Required Minimum Distributions to be made over the Designated Beneficiary's life expectancy, instead of having the 10-Year Rule apply.

In summary, Eligible Designated Beneficiaries are specified under each of the following situations:

(A) Where the Surviving Spouse of the Plan Participant is the beneficiary, either directly, or as the sole lifetime beneficiary of a Conduit Trust;

(B) Where a minor child of the Plan Participant is the beneficiary of the IRA/Plan, whether directly or as the sole lifetime beneficiary of a Conduit Trust, but only until the minor reaches age 21. Once the minor reaches age 21, the 10-Year Rule applies so that all benefits must be distributed from the IRA/Plan within 10 years of December 31st of year the minor reaches that age of majority (Note – If the Plan Participant dies after his or her Required Beginning Date, then Required Minimum Distributions will be based on the life expectancy of the Designated Beneficiary in years 1 through 9 after the minor reached age 21, with full distribution of the account occurring in year 10, at age 31 of the minor child);

(C) Where a "disabled" or "chronically ill" individual is a beneficiary of the IRA/Plan, either directly, as the sole lifetime beneficiary of a Conduit Trust, or as the sole lifetime beneficiary of an Accumulation Trust (even if the Accumulation Trust is created under a trust instrument which provides for other beneficiaries). The exception that allows the disabled or chronically ill beneficiary who is the sole lifetime beneficiary of an Accumulation Trust to qualify for the Life Expectancy Rule is unique and does not apply to other Eligible Designated Beneficiary categories;

(D) Where a beneficiary or individual is no more than 10 years younger than the Plan Participant and is a beneficiary of the IRA/Plan, either directly, or as the sole lifetime beneficiary of a Conduit Trust.

THE "AT-LEAST-AS-RAPIDLY RULE"

Note that in all situations where the deceased Plan Participant died after reaching his or her Required Beginning Date, the life expectancy of the Deceased Plan Participant may be used in lieu of the methods set forth below. The rule that allows or requires the use of the life expectancy of a deceased Plan Participant is known as the "At-Least-As-Rapidly Rule."

Beneficiary Situation	Individual Owner/Beneficiary	Conduit Trust	Accumulation Trust	Irrevocable Trust That Does Not Qualify as Conduit or Accumulation Trust, or Payable Through the Plan Participant's Estate or Another Non-Individual
Surviving Spouse Rolls Over to His or Her Own Roll-Over IRA	Can use the Surviving Spouse's Life Expectancy as if he or she were the original Plan Participant. The Required Minimum Distributions are based upon the Surviving Spouse's age under the Uniform Life Table, with annual recalculation. Required Minimum Distributions need not start until the Surviving Spouse reaches his or her Required Beginning Date.	In certain situations, the Surviving Spouse may roll over an IRA that is made payable to a Conduit Trust for the benefit of the Surviving Spouse.	N/A Surviving spouse generally is not permitted to roll over a retirement plan that is made payable to an Accumulation Trust for the benefit of the Surviving Spouse.	5-Year Rule applies, unless At-Least-As-Rapidly Rule applies.
Inherited IRA for Surviving Spouse	Required Minimum Distributions are paid over the Surviving Spouse's life expectancy under the Single Life Table (which	N/A	N/A	5-Year Rule applies, unless At-Least-As-Rapidly Rule applies.

Beneficiary Situation	Individual Owner/Beneficiary	Conduit Trust	Accumulation Trust	Irrevocable Trust That Does Not Qualify as Conduit or Accumulation Trust, or Payable Through the Plan Participant's Estate or Another Non-Individual
	is less advantageous than Uniform Life Table), with annual recalculation. The distributions must begin in the year after the death of the Plan Participant.			
Payable to Conduit or Accumulation Trust for Surviving Spouse	N/A	Same as if the Surviving Spouse inherited the IRA directly.	10-Year Rule applies.	5-Year Rule applies, unless At-Least-As-Rapidly Rule applies.
Minor Child or Conduit Trust or Accumulation Trust for Minor Child	Required Minimum Distributions are payable over life expectancy of minor child, until the child reaches age 21, based upon the child's age under the Single Life Table, without annual recalculation, and then the 10-Year Rule applies. Required Minimum Distributions must begin within the year after the death of the Plan Participant.	Required Minimum Distributions are payable over life expectancy of minor child until the child reaches age 21, and then the 10-Year Rule applies after the child reaches age 21.	10-Year Rule applies.	5-Year Rule applies, unless the Plan Participant after reaching his or her Required Beginning Date, in which event the At-Least-As-Rapidly Rule applies.
Beneficiary No More Than 10 Years Younger Than Deceased Plan Participant or Conduit or Accumulation Trust for Such Beneficiary	Required Minimum Distributions are paid over the life expectancy of the beneficiary based upon the beneficiary's age under the Single Life Table, without annual recalculation. Required Minimum Distributions must begin within the year after the death of the Plan Participant.	Required Minimum Distributions are paid over the life expectancy of the beneficiary based upon the beneficiary's age under the Single Life Table, without annual recalculation. Required Minimum Distributions must begin within the year after the death of the Plan Participant.	10-Year Rule applies.	5-Year Rule applies, unless the Plan Participant after reaching his or her Required Beginning Date, in which event the At-Least-As-Rapidly Rule applies.
Adult Beneficiary who is not (a) the Plan Participant's Surviving	10-Year Rule applies.	10-Year Rule applies.	10-Year Rule applies.	5-YearRule applies unless the Plan Participant after

Beneficiary Situation	Individual Owner/Beneficiary	Conduit Trust	Accumulation Trust	Irrevocable Trust That Does Not Qualify as Conduit or Accumulation Trust, or Payable Through the Plan Participant's Estate or Another Non-Individual
Spouse; (b) More than 10 Years Younger Than the Deceased Plan Participant; or (c) Disabled or Chronically Ill or Conduit or Accumulation Trust for such Beneficiary.				reaching his or her Required Beginning Date, in which event the At-Least-As-Rapidly Rule applies.
Disabled or Chronically Ill Beneficiary or Conduit or Accumulation Trust for Such Beneficiary	Required Minimum Distributions are paid over the life expectancy of the beneficiary based upon the beneficiary's age under the Single Life Table, without annual recalculation. Required Minimum Distributions must begin within the year after the death of the Plan Participant.	Required Minimum Distributions are paid over the life expectancy of the beneficiary based upon the beneficiary's age under the Single Life Table, without annual recalculation. Required Minimum Distributions must begin within the year after the death of the Plan Participant.	The Required Minimum Distributions can be paid over the life expectancy of the disabled or chronically ill beneficiary, but only if the disabled or chronically ill beneficiary is the sole lifetime beneficiary of the Accumulation Trust. Required Minimum Distributions must begin within the year after the death of the Plan Participant.	5-Year Rule applies unless the Plan Participant, after reaching his or her Required Beginning Date, in which event the At-Least-As-Rapidly Rule applies.

(a) The Plan Participant's Surviving Spouse. The Surviving Spouse can use the Life Expectancy Rule to take out distributions over his or her life expectancy and delay taking the first distribution from a Rollover IRA until after reaching age 72, or if the spouse elects to take the IRA/Plan as a beneficiary, distributions need not begin until the later of: (1) December 31st of the year following the Plan Participant's death; or (2) December 31st of the year in which the Plan Participant would have reached the age of 72, but only if the IRA/Plan is made payable to the spouse as a beneficiary directly, or to a Conduit Trust for the Surviving Spouse's benefit. Note that an Accumulation Trust which benefits a Surviving Spouse does not allow for the Life Expectancy Rule to apply.

(b) A Minor Child of the Plan Participant. A child of the Plan Participant under the age of majority can use the Life Expectancy Rule through reaching the age of majority, and then the 10-Year Rule applies once the child has reached the age of majority. The Proposed Regulations provide that the age of majority will be age 21. Previously the age of majority varied depending on whether a child had completed a "specified course of education."

A Conduit Trust for the benefit of the minor child is entitled to use the Life Expectancy Rule as if the IRA/Plan was payable directly to the minor child, but an Accumulation Trust which benefits such child will not qualify for the Life Expectancy Rule, so the IRA/Plan must be completely distributed within 10 years of December 31st of the calendar year in which the Plan Participant dies.

It is important to note that the minor child exception applies only to a child of the Plan Participant and does not apply to grandchildren or any other minors who might inherit the Plan Participant's IRA/Plan. Therefore, an IRA payable to a non-disabled, non-chronically ill grandchild or to a trust for a grandchild is required to be distributed to the grandchild or trust for the grandchild within 10 years of December 31st of the calendar year of the Plan Participant's death, or if payable to a trust that is not a "See-Through Trust" within 5 years or pursuant to the At-Least-As-Rapidly Rule, depending upon whether the Plan Participant died before or after his or her Required Beginning Date.

(c) Disabled Beneficiaries.

If a beneficiary is disabled as determined pursuant to Internal Revenue Code §72(m)(7), then the Life Expectancy Rule method can be used. This follows the Social Security disability definition of "disabled," and requires a very high degree of disability, as further discussed below. In order to qualify for this exception, the IRA/Plan must be payable directly to the Eligible Designated Beneficiary or to a Conduit Trust for the sole lifetime benefit of the disabled beneficiary. Additionally, the Life Expectancy Rule will apply where the IRA/Plan is made payable to an Accumulation Trust for the sole benefit of the disabled beneficiary, which is a unique exception that applies only where a beneficiary is disabled or chronically ill. Nevertheless, after the disabled beneficiary's death, the 10-Year Rule applies so that IRA/Plan benefit that was held for the disabled individual or the applicable Conduit Trust or Accumulation Trust must be distributed out of the plan within 10 years of December 31st of the calendar year in which the disabled beneficiary dies.

A beneficiary qualifies as a disabled beneficiary if a determination of the same has been made by the Social Security Agency or if the individual qualifies pursuant to the either of the definitions of "disabled" provided below. The age of the beneficiary determines which definition of "disabled" must be applied. If the beneficiary is over the age of 18, the Social Security definition of "disabled" is used. Internal Revenue Code Section 72(m)(7) and the applicable regulations provide that "an individual shall be considered to be disabled if he is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or to be of long-continued and indefinite duration. An individual will not be considered to be disabled unless he furnishes proof of the existence thereof in such form and manner as the Secretary may require."

However, if the beneficiary is under the age of 18, the individual must be proven to "[have] a medically determinable physical or mental impairment that results in marked and severe functional limitations and … can be expected to result in death or to be of long and continued and indefinite duration."

Treasury Regulation Section 1.72-17A(f) states that under Section 72(m)(7), "when determining whether an individual's impairment makes him unable to engage in any substantial gainful activity, by reason of any medically determinable physical or mental impairment which can be expected to result in death or be of long-continued and indefinite duration. In determining whether an individual's impairment makes him unable to engage in any substantial gainful activity, primary consideration shall be given to the nature and severity of his impairment." Additionally, "consideration shall also be given to other factors such as the individual's education, training, and work experience." The substantial gainful activity to which Internal Revenue Code §72(m)(7) refers is "the activity, or a comparable activity, in which the individual customarily engaged prior to the arising of the disability or prior to retirement if the individual was retired at the time the disability arose."

Further, this Regulation states that in order to meet the requirements of Section 72(m)(7), "an impairment must be expected either to continue for a long and indefinite period or to result in death." The term "indefinite" is used in the sense that it "cannot reasonably be anticipated that the impairment will, in the foreseeable future, be so diminished as no longer to prevent substantial gainful activity." An individual will not be deemed disabled if, "with reasonable effort and safety to himself, the impairment can be diminished to the extent that the individual will not be prevented by the impairment from engaging in his customary or any comparable substantial gainful activity."

Treasury Regulation Section 1.72-17A(f) also provides the following examples of impairments which would ordinarily be considered as preventing an individual from engaging in substantial gainful activity. It is noteworthy that the existence of one or more of the following impairments, or an impairment of greater severity, does not guarantee that there will be a finding that an individual is disabled:

(i) Loss of use of two limbs;

(ii) Certain progressive diseases which have resulted in the physical loss or atrophy of a limb, such as diabetes, multiple sclerosis, or Buerger's disease;

(iii) Diseases of the heart, lungs, or blood vessels which have resulted in major loss of heart or lung reserve as evidenced by X-ray, electrocardiogram, or other objective findings, so that despite medical treatment breathlessness, pain, or fatigue is produced on slight exertion, such as walking several blocks, using public transportation, or doing small chores;

(iv) Cancer which is inoperable and progressive;

(v) Damage to the brain or brain abnormality which has resulted in severe loss of judgment, intellect, orientation, or memory;

(vi) Mental diseases (e.g. psychosis or severe psychoneurosis) requiring continued institutionalization or constant supervision of the individual;

(vii) Loss or diminution of vision to the extent that the affected individual has a central visual acuity of no better than 20/200 in the better eye after best correction, or has a limitation in the fields of vision such that the widest diameter of the visual fields subtends an angle no greater than 20 degrees;

(viii) Permanent and total loss of speech; and/or

(ix) Total deafness uncorrectable by a hearing aid.

To qualify as a Disabled Beneficiary, the beneficiary must qualify pursuant to one of the three definitions prior to the date of death of the Plan Participant.

If a beneficiary is disabled as determined by any of the three aforementioned definitions, the Life Expectancy Rule can be utilized. The IRA/Plan can be payable either directly to the Eligible Designated Beneficiary or to a Type II Multi-Beneficiary Trust.

A Multi-Beneficiary Trust is a "see-through trust with more than one beneficiary and with respect to which— (i) All of the trust beneficiaries are [D]esignated [B]eneficiaries; and (ii) At least one of the trust beneficiaries is an [E]ligible [D]esignated [B]eneficiary who is disabled . . . or chronically ill." There are two types of Multi-Beneficiary Trusts: Type I and Type II. A Type I Multi-Beneficiary Trust is a trust where "the terms . . . provide that it is to be divided immediately upon the death of the employee into separate trusts for each beneficiary." A trust is considered a Type II Multi-Beneficiary Trust when all of the following apply: "(A) The trust terms identify one or more individuals, each of whom is disabled . . . or chronically ill . . ., who are entitled to benefits during their lifetime; and (B) The terms of the trust provide that no individual . . . [other than the Disabled/Chronically Ill Beneficiary] has any right to the employee's interest in the plan until the death of all of the [E]ligible [D]esignated [B]eneficiaries." As to Type II Multi-Beneficiary Trusts, the presence of non-Eligible Designated Beneficiaries will not prevent the application of the Life Expectancy Rules. Therefore, the trust could provide for the benefit of non-Eligible Designated Beneficiaries permitted that such beneficiaries are only entitled to benefits following the death of the Disabled Beneficiary.

Nevertheless, after the disabled beneficiary's death, the 10-Year Rule applies so that IRA/Plan benefit that was held for the disabled individual or the applicable Type II Multi-Beneficiary Trust must be distributed out of the plan within 10 years of December 31st of the calendar year in which the disabled beneficiary dies.

(d) Chronically Ill Individuals.

Likewise, if a beneficiary is "chronically ill," then the Life Expectancy Rule will apply in the same manner as provided above, and the 10-Year Rule will apply after the death of such chronically ill individual. As with disabled beneficiaries, the chronically ill exception applies if the IRA/Plan is made payable directly to the chronically ill beneficiary, or to a Type II Multi-Beneficiary Trust for the sole lifetime benefit of the chronically ill individual.

By definition, a chronically ill beneficiary is:

> any individual who has been certified by a licensed health care practitioner as [one of the following]—
>
> (1) being unable to perform (without substantial assistance from another individual) at least 2 activities of daily living for a period of at least 90 days due to a loss of functional capacity,
>
> (2) having a level of disability similar (as determined under regulations prescribed by the Secretary in consultation with the Secretary of Health and Human Services) to the level of disability described in clause (1), or
>
> (3) requiring substantial supervision to protect such individual from threats to health and safety due to severe cognitive impairment.

It is ironic that the definition of disability from the Social Security law can be used to satisfy the definition of chronically ill individual but is not used in the definition of disability itself under the SECURE Act. This may have been inadvertent.

A licensed health care practitioner must certify that such individual meets such requirements within the preceding 12-month period, so certification must occur annually and is crucial.

(e) A Beneficiary Less than 10 Years Younger than the Plan Participant.

The Life Expectancy Rule also applies where an IRA/Plan is made payable to an individual (or to a See-Through Trust for the sole lifetime benefit of an individual) who is not more than 10 years younger than the Plan Participant. However, the 10-Year Rule will apply upon the death of such beneficiary.

The determination of whether a beneficiary is not more than 10 years younger is made upon the actual birth dates of the Plan Participant and beneficiary rather than the calendar years in which each was born.

Therefore, it is advantageous for a Plan Participant to leave IRA/Plan assets to a beneficiary who is less than 10 years younger than him or her, assuming that the beneficiary's life expectancy is well over 10 years.

Now That We Understand the Rules, What Do We Do?

a. When the Surviving Spouse is the Beneficiary.

For most married couples, the question in IRA inheritance planning is how to best benefit the Surviving Spouse while deferring income taxes, saving the inheritance from a subsequent spouse, creditors, or other threats to wealth, and giving the Surviving Spouse reasonable control without over-complicating the situation. When one spouse dies leaving the other spouse or a trust for the spouse as a beneficiary, one of the following four scenarios will apply:

i. *Spousal Rollovers Still Work Fine.*

A common approach is for the Plan Participant to leave IRA/Plans solely to his or her Surviving Spouse. This will enable the Surviving Spouse to roll over all or any portion of the IRA/Plan into the Spouse's own IRA. The Surviving Spouse then will be treated as if he or she were the original Plan Participant of the rolled over IRA, which allows the Surviving Spouse to delay required distributions from the IRA until after he or she has reached the age of 72, and to take Required Minimum Distributions over the more favorable "Uniform Life" distribution table. It also allows the Surviving Spouse to select the beneficiary who will inherit the IRA upon his or her later death.

The Spouse can roll the account balances to his or her own "rollover IRA," and will not need to begin taking distributions until April 1st of the year following the year in which the Surviving Spouse reaches age 72. The IRA will be treated exactly as if it was the Surviving Spouse's IRA from inception.

The downsides of the spousal IRA rollover include the uncertainty or problematic probabilities that the spouse may overspend the IRA, invest unwisely, or leave the IRA to one or more individuals or entities not favored by the Plan Participant.

ii. *Inherited IRAs Still Work Fine.*

The Surviving Spouse can also decide to become the beneficiary of the IRA in lieu of rolling over the IRA into his or her own IRA. If the Spouse decides to keep the IRA in place and simply be the beneficiary (this is often referred to as an “Spousal Inherited IRA”), then the Life Expectancy Rule can be used, and distributions will be made from the IRA based upon the Surviving Spouse’s remaining life expectancy. If the Surviving Spouse takes the IRA as a beneficiary, then Required Minimum Distributions must begin by the later of: (1) December 31st of the year following the year of the decedent's death; or (2) December 31st of the year in which the deceased Plan Participant would have reached age 72, regardless of Surviving Spouse's age.

A Surviving Spouse who has not yet reached the age of 59½ and needs to withdraw from the IRA/Plan will need to take the IRA/Plan as a beneficiary (rather than rolling it over) in order to avoid imposition of the 10% excise tax that applies if and when a Plan Participant withdraws assets from his or her Non-Roth IRA/Plan prior to attaining the age of 59½. Alternatively, the Surviving Spouse may “annuitize” a rollover IRA by investing the IRA assets in an annuity contract whereby the insurance carrier issuing the contract will make a series of equal annual or more frequent lifetime payments to the IRA owner. These payments will be considered to satisfy the Required Minimum Distributions, and neither of the payments nor the value of an annuitized annuity will be aggregated with any other IRA/Plan for purposes of calculating the Required Minimum Distributions. The annuitized payments will typically exceed the Required Minimum Distributions that would have applied.

iii. *At First Blush, the Spousal Conduit Trust Looks More Attractive Than Under Prior Law, But Is It Really?*

A Conduit Trust is a trust that is named as the beneficiary of the IRA/Plan that is required under the trust agreement to pay the Designated Beneficiary (in this case the Surviving Spouse) exactly what is distributed from the IRA/Plan account, without delay, regardless of whether the Spouse needs the money, or might even have to give a required distribution to a creditor.

This at least protects the part of the IRA/Plan that has not been distributed and allows the trustee of the trust to take out distributions using the life expectancy of the Surviving Spouse, recalculated annually.

In a second marriage situation or other circumstances where the Plan Participant wants the Surviving Spouse to have the lifetime benefit of an IRA/Plan, but not the ability to choose the beneficiary thereof after the spouse's death, a Conduit Trust for the lifetime benefit of the Surviving Spouse might be the best alternative. The Conduit Trust can be drafted to provide for whatever remains in the IRA/Plan to be held in the Trust for the Plan Participant's desired secondary beneficiaries after the Surviving Spouse's death, but the 10-Year Rule will apply after the Surviving Spouse's death to require *that all assets be distributed from the IRA/Plan within approximately 11 years after the Surviving Spouse's death.*

If the Surviving Spouse has reached age 72, and thus already required to take out Required Minimum Distributions from his or her own IRA, then the tax impact and the timing of Required Minimum Distributions to the Spouse are almost as good under the Conduit Trust as it will be in a rollover IRA, but the principal and management of the IRA might be better protected.

Additionally, using a Conduit Trust causes Required Minimum Distributions to be distributed out of the Trust to the applicable Designated Beneficiary, which means that any such distributions will not be protected from creditors or unwise spending of the beneficiary.

Because of these rules, many couples who would otherwise use rollover IRAs or Conduit Trust IRA/Plan arrangements may consider the use of an Accumulation Trust described below, and sacrifice an increase in taxes, particularly in situations where the Spouse can benefit from additional protection from creditors, future spouses, possible dementia, and otherwise.

It is unknown whether a trust that initially qualifies as a Conduit Trust and is later "amended" by a state court proceeding, decanting, or an Action By Trust Protectors who have no fiduciary duties, in order to require that an IRA/Plan distribution not be paid to a beneficiary, will cause retroactive disqualification and penalties for having considered such trust to have been a Conduit Trust from inception. It seems likely to the authors that many taxpayers will "take their chances" on or before the time when a large distribution has to be made, if the beneficiary would otherwise lose or would be sure to misspend large distributions, which may cause the tax due on such amounts to become uncollectible from an IRS standpoint.

iv. *The Spousal Accumulation Trust – 10-Year Rule Must Apply.*

An Accumulation Trust is a trust that can receive distributions from the IRA/Plan and accumulate them without having to pay them directly to a particular beneficiary. Typically, the trustee of an

Accumulation Trust has the power to withhold distributions or to make them as needed for the health, education, maintenance and support of the spouse and common descendants of the spouse and the Grantor. Fortunately, the 2022 Proposed Regulations indicate that if an Accumulation Trust includes only Eligible Designated Beneficiaries as Tier I Beneficiaries and Tier II Beneficiaries (such as if the Surviving Spouse is the sole beneficiary of an Accumulation Trust with the remainder to go outright to the Plan Participant's brother who is not more than ten years younger than the Plan Participant), then the Life Expectancy Rule will apply in lieu of the 10-Year Rule. Nevertheless, careful drafting will be necessary to ensure that this special treatment applies, and it is not clear whether this provision will make it into the Final Regulations (although it is very likely given that it is taxpayer-friendly).

At worst, the new law permits distributions from the IRA/Plan held under an Accumulation Trust to be delayed under the 10-Year Rule.

If a Trust does not qualify as a See-Through Trust (either a Conduit Trust or an Accumulation Trust), then the 5-Year Rule applies, unless the Plan Participant died after his or her Required Beginning Date, in which event the At-Least-As-Rapidly Rule will apply.

b. <u>When an Adult Non-Spouse Individual Who is Not Disabled, Chronically Ill, or Less Than Ten Years Younger Than the Plan Participant is the Beneficiary</u>.

The choices here are simple. If there is no Eligible Designated Beneficiary as the beneficiary of the IRA/Plan, then the 10-Year Rule will likely apply, regardless of whether IRA/Plan benefits are left to the beneficiary directly, through a Conduit Trust, or through an Accumulation Trust.

There is one notable exception to the above. If the Plan Participant died after his or her Required Beginning Date (meaning that Required Minimum Distributions were required prior to the Plan Participant's death), then the beneficiary will be able to continue taking Required Minimum Distributions based upon the life expectancy of the deceased Plan Participant under the At-Least-As-Rapidly Rule, which can be beneficial in situations where the Plan Participant died shortly after reaching the age of 72 due to the fact that the deceased Plan Participant's life expectancy could be longer than 10 years.

Under prior law, if a Plan Participant died after reaching his or her Required Beginning Date, then the beneficiaries would be entitled to the benefit of the At-Least-As-Rapidly Rule to cause Required Minimum Distributions to be payable over the deceased Plan Participant's life expectancy, based upon the single life table, without annual recalculation. There was some question (at least until the Proposed Regulations were issued) as to whether the At-Least-As-Rapidly Rule continues to apply where an IRA/Plan is left to an individual Designated Beneficiary or to a trust that qualifies as a See-Through Trust (i.e. a Conduit Trust or an Accumulation Trust) under the SECURE Act. The 2022 Proposed Regulations clarified that the At-Least-As-Rapidly Rule will continue to apply.

Treasury Regulation Section 1.401(a)(9)-5, Q&A-5 discusses the determination of the distribution period to apply if the Plan Participant dies on or after his or her Required Beginning Date by indicating that the longer of: (i) the life expectancy of the Designated Beneficiary (which no longer applies under the SECURE Act unless the beneficiary is an Eligible Designated Beneficiary); or (ii) the deceased Plan Participant's remaining life expectancy, as if he or she was still living.

A Designated Beneficiary of an IRA/Plan still has the ability to use the At-Least-As-Rapidly Rule if the Plan Participant dies on or after his or her Required Beginning Date because Internal Revenue Code Section 401(a)(9)(B)(i)(II) was not modified by the SECURE Act to modify or remove the "At-Least-As-Rapidly Rule," and nothing in the revised statute indicates that the 10-Year Rule was intended to eliminate the "At-Least-As-Rapidly Rule" or change the default distribution period applicable where the Plan Participant dies on or after his or her Required Beginning Date.

While Internal Revenue Code Section 401(a)(9)(H)(i)(II) indicates that the 10-Year Rule applies in lieu of the 5-Year Rule where there is a Designated Beneficiary, regardless of whether the Plan Participant died on or after his or her Required Beginning Date, if Congress intended to remove the At-Least-As-Rapidly Rule, then Section 401(a)(9)(B)(i)(II) would have been modified accordingly. The objective of Internal Revenue Code Section 401(a)(9)(H)(i)(II) appears to be to replace the 5-Year Rule with the 10-Year Rule where a Plan Participant dies and leaves a (non-eligible) Designated Beneficiary, even if the Plan Participant dies on or after his or her Required Beginning Date.

Further, if this Section is read in conjunction with the post-SECURE Act Internal Revenue Code Section 401(a)(9), it seems that the "longer of" the deceased Plan Participant's remaining life expectancy, or the distribution period applicable to the Designated Beneficiary (whether it be the Life Expectancy Rule if the Designated Beneficiary is an Eligible Designated Beneficiary, or the 10-Year Rule otherwise) will apply if Plan Participant died on or after his or her Required Beginning Date.

The solution is easier if a trust is the beneficiary of the Plan, as the choice can be made by intentionally failing to comply with the requirement that certain documentation be provided to the plan administrator by October 31st of the year after the Plan Participant's death.

It also does not seem that Congress wanted to provide less flexibility for individual Designated Beneficiaries, rather than for situations where the Designated Beneficiary is determined under a See-Through Trust or if there is no Designated Beneficiary, as it is clear that the At-Least-As-Rapidly Rule will apply if there is no Designated Beneficiary. Additionally, the At-Least-As-Rapidly Rule would not change the distribution period that would apply if the Plan Participant were still living, so the distribution period would not be extended by reason of the Plan Participant's death, which leads to conclusion that it was intended to remain in effect where there is a Designated Beneficiary of the IRA/Plan.

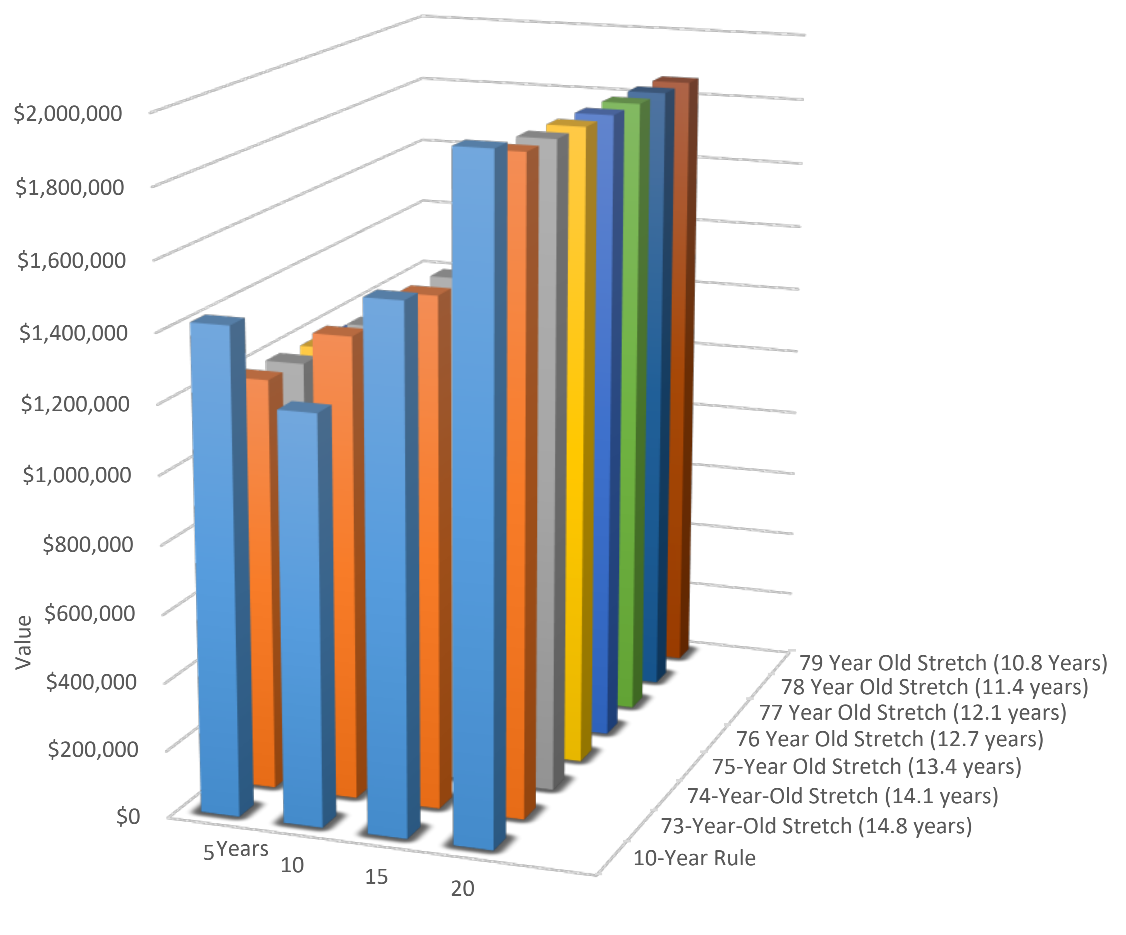
Planners should consider this and run the numbers as numerous factors weigh into this decision. Regardless of whether the At-Least-As-Rapidly Rule applies where there is a Designated Beneficiary of an IRA/Plan, the difference is less pronounced than might initially be understood.

For example, the attached chart illustrates a comparison of the application of the 10-Year Rule versus the At-Least-As-Rapidly Rule where a Plan Participant dies after reaching his or her Required Beginning Date and leaves the IRA/Plan to a non-spouse beneficiary who is not an Eligible Designated Beneficiary.[110] For the purposes of this example, the IRA balance upon the death of the Plan Participant is $1,000,000, and the assumed growth of the assets under the IRA are 6% per year and 5% per year for assets outside of the IRA. As indicated by the attached chart, the amount of assets left after 20 years is actually greater under the 10-Year Rule approach, as opposed to under the At-Least-As-Rapidly Rule, due to the effect of the time value of money based upon the Required Minimum Distributions because Required Minimum Distributions can be deferred until the 10th year following the Plan Participant's death, while the At-Least-As-Rapidly Rule would require payments of the Required Minimum Distributions annually beginning in the year following the Plan Participant's death.

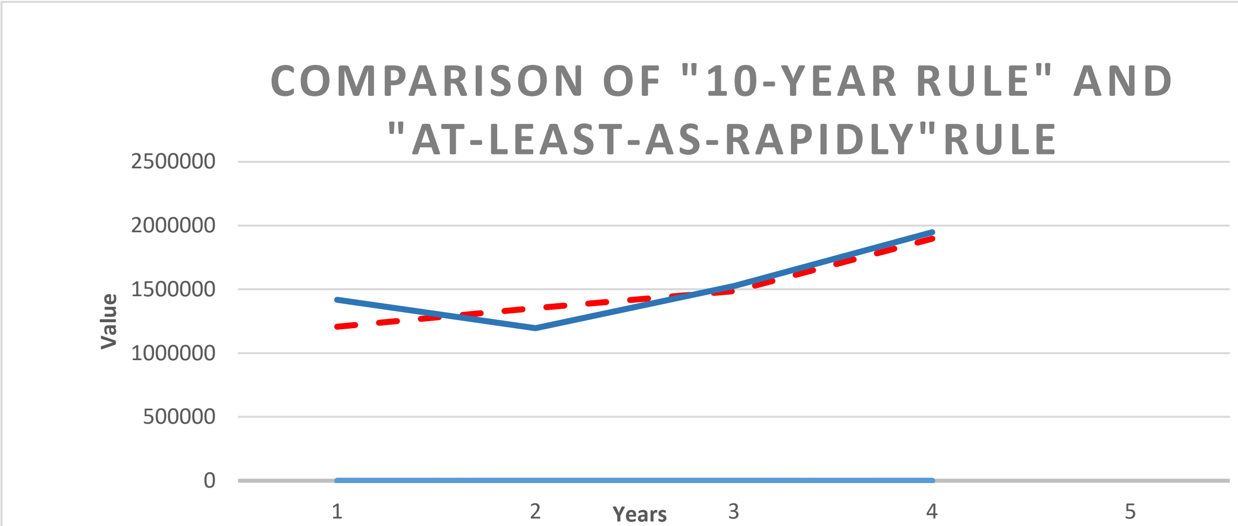
The results are illustrated as follows:

[110] Note that the numbers are not updated to account for changes in the mortality tables that have occurred since 2020. The numbers also do not account for changes that would be made by the Proposed Regulations released in 2022. The tables will be updated when the Final Regulations are released.

COMPARISON OF THE "10-YEAR RULE" AND THE "AT-LEAST-AS-RAPIDLY RULE"



	5	10	15	20	
10-Year Rule	$1,418,519	$1,195,928	$1,526,341	$1,948,041	
73-Year-Old Stretch (14.8 years)	$1,207,460	$1,352,722	$1,486,692	$1,897,438	
74-Year-Old Stretch (14.1 years)	$1,196,830	$1,324,352	$1,481,523	$1,890,841	
75-Year Old Stretch (13.4 years)	$1,185,067	$1,292,733	$1,476,444	$1,884,358	
76 Year Old Stretch (12.7 years)	$1,171,981	$1,257,195	$1,471,271	$1,877,756	
77 Year Old Stretch (12.1 years)	$1,159,531	$1,222,911	$1,466,860	$1,872,127	
78 Year Old Stretch (11.4 years)	$1,143,307	$1,177,152	$1,461,860	$1,865,745	
79 Year Old Stretch (10.8 Years)	$1,127,679	$1,141,928	$1,457,422	$1,860,081	



The life expectancy that applies where the At-Least-As-Rapidly Rule is used is as follows, and in each case the distribution percentage would be calculated by taking the applicable divisor and reducing it by one in each year after the first year of the Plan Participant's death:

LIFE EXPECTANCY UNDER THE AT-LEAST-AS-RAPIDLY RULE

Ages 74-81	
73	15.5 years
74	14.1 years
75	13.4 years
76	12.7 years
77	12.1 years
78	11.4 years
79	10.8 years
80	10.2 years
81 +	Less than 10 years

The above rules will also apply to a minor child if the Plan Participant was not his or her parent (such as a grandchild, niece or nephew, or unrelated person).

c. When a Minor Child of the Plan Participant is a Beneficiary.

When a minor child of the deceased Plan Participant is the sole beneficiary of the IRA, then the Life Expectancy Rule will apply to require very small distributions each year until the minor child reaches age 21, and after that it was thought that no distributions would need to be made until December 31st of the 10th calendar year after the child reaches age 21 under the 10-Year Rule.

The 2022 Proposed Regulations discussed in Chapter 8 caught many by surprise by providing that Required Minimum Distributions based on the life expectancy of the now adult child would continue after the child reaches age 21, and the entire account would be distributed no later than December 31st of the 10th calendar year after the child reaches age 21.

The same analysis applies if the minor child is the beneficiary of a Conduit Trust. Accordingly, the Life Expectancy Rule can be used until the child reaches age 21, at which time the 10-Year Rule will apply and the entire IRA/Plan must be distributed within approximately10 years.

The payout percentages for a minor are very low, as reflected below:

PAYOUT PERCENTAGES FOR A MINOR

Ages 1-13		Ages 14-26	
1	1.23%	14	1.45%
2	1.24%	15	1.47%
3	1.25%	16	1.49%
4	1.27%	17	1.52%
5	1.29%	18	1.54%
6	1.30%	19	1.56%
7	1.32%	20	1.59%
8	1.34%	21	1.61%
9	1.36%	22	1.64%
10	1.37%	23	1.66%
11	1.39%	24	1.69%
12	1.41%	25	1.72%
13	1.43%	26	1.75%

It is not clear whether there can be one Conduit Trust for multiple minors or whether there will have to be a separate trust for each minor child. It is likely that if all beneficiaries are minors then the Life Expectancy Rule can be used based upon the age of the oldest trust beneficiary, and once the oldest trust beneficiary reaches age 21, the 10-Year Rule will apply. This question will likely be addressed in future Treasury Regulations or other pronouncements. Until then, it will be safest to have an IRA/Plan payable to separate subtrusts for each minor which can come into existence under the will or a trust on the death of the Plan Participant so that there is a separate trust for each minor beneficiary which can receive distributions from a separate IRA/Plan, or a percentage of distribution rights.

For example, instead of leaving an IRA payable by beneficiary designation to a client's living trust which then divides into separate trusts for the children, the beneficiary designation of the IRA can provide for 20% of the IRA/Plan to be payable to each of five separate irrevocable trusts for the five separate children, each of which are established under the client's living trust agreement. Many commentators believe that the prior law provides that an IRA could be made payable by a beneficiary designation on a percentage basis to separate subtrusts and that this would consider each separate portion of the IRA to be treated as if a separate IRA had been made payable to such separate trust.

If the IRA is made payable to an Accumulation Trust for minors, then the 10-Year Rule will apply. Therefore, clients will have to decide whether the tax deferral afforded by leaving the IRA/Plan directly to a minor beneficiary or to a Conduit Trust for a minor beneficiary is more important than protecting the assets by having them payable to an Accumulation Trust for the beneficiary's lifetime. Obviously, the income tax results are more favorable if the IRA/Plan is left directly to or in a Conduit Trust for a minor child, but this approach will cause the IRA benefits to be paid out to the child no later than then 10 years after the child reaches age 21, which could subject such assets to unwise spending, the child's creditors and/or possible future divorcing spouses. Additionally, clients will have to assure that their estate plan is appropriately coordinated so that any IRA/Plan benefits that would be left to or for a minor child or to a Conduit Trust for the benefit of a child while the child is a minor will be switched to an Accumulation Trust (if possible) for the benefit of the child after the child reaches age 21.

However, for most clients, it is best to not let the "tax tail wag the dog" where there is real concern that any IRA/Plan assets that are left directly to a child (or to a Conduit Trust for the child) would cause loss of such assets or would subject any such assets to the child's creditors or other threats to wealth.

A preferable approach is leaving the assets to an Accumulation Trust for the benefit of the child despite the fact that such approach would be subject to the 10-Year Rule at best (as opposed to the Life Expectancy Rule that could be achieved by leaving the IRA/Plan directly to the minor child or to a Conduit Trust for the minor child), if the IRA/Plan benefits would be unwisely or improperly spent by the minor child, or subject to the minor child's creditors or other threats to wealth when the assets are distributed from the IRA/Plan. This is akin to a 100% tax!

CHOICES FOR MINOR IRA OR PENSION BENEFICIARY

"Don't handicap your children by making their lives easy." **– Robert A. Heinlein**

	Payout Method to Apply	Advantages	Disadvantages[111]
1. Outright to Child	Over life expectancy, until child reaches age of majority – then 10-Year Rule applies – measured fromage of majority, as determined under state law	Simple, but may require appointment of guardian.	May result in loss, based upon poor judgment, creditor access,eventual divorce, etc.

[111] This chart is also included in this Book on page 171.

	Payout Method to Apply	Advantages	Disadvantages[111]
2. To Custodian under Uniform Gift to Minors Act, or Equivalent State Law	Tax treatment same as #1 above.	The IRA/Plan and funds will be protected from indiscretion of the child until reaching the age that the child can take the arrangement over.	The child can take the arrangement over at a relatively young age (often 25), and creditorsof the child,divorcing spouses, etc., can reach the accounts atall ages.
3. Conduit Trust	Tax treatment same as #1 above. Could be payableto a Custodian of a Uniform Transfers to Minors Act account for a minor beneficiary.	Protects the principal of the IRA/Plan from indiscretion and creditors until 10 years after the child reaches age 21.	Expense of administering Conduit Trust, and requirement that all Required Minimum Distributions must be paid to child or Custodian (based upon life expectancy until ten years after reaching age of majority), and then everything must be paid out
4. Accumulation Trust	10-Year Rule will apply – shortest payout of all alternatives.	Trustee can completely control if and when there will be withdrawals from the IRA/Plan, and if and when there will bedistributions to the child, if any.	Shorter payout, and expenses of operating Accumulation Trust.
5. TEA POT Trust – For Minor Beneficiary and Other Beneficiaries	Same as for #4 above.	Trustee can decide if and when the minor or other beneficiaries are mostdeserving, in need, or at lowest tax brackets.	Trustee discretion may disappoint the beneficiary – best to have a separate Equalization Trust and responsible Trustees.

SPECIAL BENEFICIARY ARRANGEMENTS FROM A CREDITOR PROTECTION STANDPOINT

Method of Distribution	Payout/ Taxation	Protection Under the Best State Laws*	Less Protective States*	In Bankruptcy*
Payment to an Accumulation Trust for Disabled or Chronically Ill Beneficiary	Life Expectancy	Protected from Creditors	Protected from Creditors – May disqualify from some forms of public aid.	Protected as a legitimate Third-Party Spendthrift Trust, if properly drafted
Conduit Trust for Not More Than 10-Year-Older Beneficiary	Life Expectancy	Payments Not Protected	Payments Not Protected	Not Protected
Accumulation Trust for Beneficiary Not More Than 10 Years Younger	10-Year Rule	Payments Well Protected	Payments Well Protected	Protected from Creditors

*Debtors residing in many states will be able to use the better of the state law or the bankruptcy law upon filing bankruptcy.

NOTE: Only Accumulation Trusts will be completely protected from Super Creditors – the IRS, the FTC, the SEC, criminal restitution, and some Medicare responsibilities. Only Accumulation Trusts may be protected from Exception Creditors (spouses, ex-spouses, child support, divorce attorney's fees and legal and associated costs incurred by a beneficiary who is not able to pay them), depending upon state law (Nevada and South Dakota do not allow Exception Creditors to reach into an asset protection trust).

d. When a Chronically Ill or Disabled Individual is the Beneficiary

If an IRA/Plan is made payable directly, or through a Conduit Trust, to a chronically ill or disabled beneficiary then the Life Expectancy Rule is used to calculate Required Minimum Distributions.

Additionally, an Accumulation Trust for a chronically ill or disabled beneficiary will qualify under the Life Expectancy Rule for a payout over the life expectancy of the chronically ill or disabled beneficiary, as long as he or she is the sole lifetime beneficiary of the trust.

This is the only situation in which an Accumulation Trust can qualify for the Life Expectancy Rule.

Further, if an IRA/Plan is made payable to a trust that subsequently divides into separate trusts for the sole lifetime benefit of a chronically ill or disabled beneficiary, then the Life Expectancy Rule will also apply.

For example, if the IRA was made payable to a trust that subsequently divided into two trusts, one for the sole benefit of the Surviving Spouse, and the other trust for the sole benefit of a chronically ill beneficiary, then the trust for the Surviving Spouse, regardless of whether it is a Conduit Trust or Accumulation Trust, would be subject to the 10-Year Rule; however the trust for the benefit of the chronically ill beneficiary could qualify for the Life Expectancy Rule, regardless of whether the trust is a Conduit Trust or an Accumulation Trust.

Planners will still need to consider the Separate Share Rule and whether trusts will need to be funded separately and directly with IRA benefits in order to achieve the desired distribution period for Required Minimum Distribution purposes ("Destination Trust"), or whether they can be funded from the division of a trust that can be named as the beneficiary of the IRA/Plan (a "Funding Trust").

The Separate Share Rule allows separate trusts that are funded from a single IRA/Plan to be considered as having been funded separately and will only apply in certain circumstances. Prior to the SECURE Act (i.e., if the Plan Participant dies before January 1, 2020), this applied as long as the IRA/Plan is divided into separate IRA/Plans, with each applicable separate Destination Trust being named as the beneficiary of the corresponding separate IRA/Plan under the beneficiary designation. Each trust (at the time it receives benefits) must be a separate trust under applicable state law with its own taxpayer identification number. If the Plan Participant died on or after January 1, 2020, then the Separate Share Rule may still be applicable if the IRA/Plan is made payable to separate trusts for separate Eligible Designated Beneficiaries, although this is not clear because the Treasury Regulations are inconsistent with the statute following the SECURE Act. The following chart illustrates when an IRA/Plans must be payable directly to the "Destination Trust" or whether it can flow through a "Funding Trust."

WHEN IRA/PLAN PAYS TO "DESTINATION TRUST" OR "FUNDING TRUST"

Type of Destination Trust	Payable Directly to Destination Trust or Can Be Payable to Funding Trust?
Conduit Trust for the benefit of the Surviving Spouse.	Must be payable to Destination Trust in order to get benefit of Life Expectancy Rule (or else 10-Year Rule applies); although it is not clear, and further guidance is needed.
Conduit Trust for the benefit of the minor child.	Must be payable directly to Destination Trust in order to get benefit of Life Expectancy Rule (or else 10-Year Rule applies); although it is not clear, and further guidance is needed.

Type of Destination Trust	Payable Directly to Destination Trust or Can Be Payable to Funding Trust?
Conduit Trust for the benefit of a beneficiary who is no more than 10 year younger than Participant.	Must be payable directly to Destination Trust in order to get benefit of Life Expectancy Rule (or else 10-Year Rule applies); although it is not clear, and further guidance is needed.
Conduit Trust or Accumulation Trust for a Disabled or Chronically Ill Beneficiary.	Can be payable directly to Destination Trust or to Funding Trust, although if payable to Funding Trust, then Destination Trust must be created upon the death of the deceased Plan Participant.
Conduit Trust for Non-Eligible Designated Beneficiary	Does not matter whether payable directly to Destination Trust or to a FundingTrust (10-Year Rule applies regardless).
Accumulation Trust for a Beneficiary who is not Chronically Ill or Disabled.	Does not matter whether payable directly to Destination Trust or to a Funding Trust (10-Year Rule applies regardless).

e. When a Non-Spouse Not More Than Ten Years Younger than the Plan Participant is a Beneficiary

The final exception to the 10-Year Rule applies when a non-spouse individual who is not more than 10 years younger than the Plan Participant is the sole beneficiary of the IRA/Plan. In this case, the Life Expectancy Rule can be used if the IRA/Plan is made payable to such beneficiary directly or through a Conduit Trust.

This exception does not apply when the IRA/Plan is made payable to an Accumulation Trust for the benefit of such Individual, and the 10-Year Rule will apply instead.

As discussed above, if the Plan Participant died after the Required Beginning Date (meaning that Required Minimum Distributions were required prior to the Plan Participant's death), then the beneficiary or Trustee of the Conduit Trust can elect to continue taking Required Minimum Distributions based upon the life expectancy of the deceased Plan Participant, which would be beneficial in cases where the beneficiary is older than the Plan Participant.

Trust Drafting Considerations

Lawyers and advisors drafting trust documents have many strategies to consider, going well beyond having language which qualifies for the basic requirements of having one or more trusts that will be properly funded and established to qualify as See-Through Trusts. Specifically, lawyers and advisors should consider whether to draft for Accumulation Trusts to provide for life expectancy payments for a disabled or chronically ill beneficiary and a 10-year payout for all other individual beneficiaries, or for Conduit Trusts which can provide for life expectancy payments for a Surviving Spouse or a beneficiary who is not more than 10 years younger than the Plan Participant. A Conduit Trust could also provide a life expectancy payout for a minor child of the deceased Plan Participant until reaching age 21 or completion of a prescribed course of education, with the 10-Year Rule to apply thereafter.

Beyond the question of whether an Accumulation Trust or a Conduit Trust arrangement is in the best interests of primary and remainder beneficiaries, the technical drafting for such arrangements can be both challenging and complicated.

Planners are well advised to review attorney Steven B. Gorin's white paper entitled *Drafting Under the SECURE Act* that was presented in a LISI Webinar of that name on February 28, 2020. The authors thank Steven Gorin and also Natalie Choate for this excellent white paper, which includes excerpts from Natalie Choate's January 30, 2020 ACTEC/ALI-CLE webinar of February 13, 2020 concerning "Auto Switch" and "Toggle" provisions. Steve Gorin can be reached at **sgorin@thompsoncoburn.com** and can provide those who request it with his over 2,300 page, fully searchable PDF, that is updated quarterly and entitled *Structuring Ownership of Privately-Owned Businesses; Tax and Estate Planning Implications*. This resource can also be obtained at http://www.thompsoncoburn.com/forms/gorin-newsletter.

Natalie Choate's website is **http://www.ataxplan.com**, and the online version of her book entitled *Life and Death Planning for Retirement Benefits* can be purchased at **https://retirementbenefitsplanning.us** for $9 per month (cancel at any time).

A significant topic discussed in the above materials is whether trusts should have "Auto Switches," toggle provisions, or a combination of the two.

An example of an "Auto Switch" would be language that would cause an Accumulation Trust, intended to be established for a significant other of a Plan Participant, to automatically become a Conduit Trust for a Surviving Spouse if the Plan Participant and the significant other marry before the Plan Participant's death.

Another example is where a trust agreement would provide for the division of IRA/Plan assets into separate trusts for the benefit of the Plan Participant's children in a manner that would cause the 10-Year Rule to apply. Between the time of signing trust documents and the death of the Plan Participant, a child may have become disabled or chronically ill and would benefit from having the trustee be able to take distributions ratably over the beneficiary's lifetime by having the trust provide that the applicable child be the sole lifetime beneficiary who can receive distributions or benefits during his or her lifetime so as to cause the trust for such child to qualify for life expectancy payouts of Required Minimum Distributions.

An "Auto Switch" provision would include the appropriate technical language so that in the event that the primary beneficiary of any trust herein established is disabled or chronically ill, as such conditions are defined under the SECURE Act. Further, the provision would state that, if such trust is the beneficiary of an IRA/Plan, then such trust shall be considered to be amended no later than September 30th of the year following the death of the Plan Participant to provide that the primary beneficiary shall be the sole beneficiary who may receive distributions or benefits during his or her lifetime, or until he or she is no longer disabled or chronically ill, in order to qualify such trust to be treated as an Accumulation Trust for such Disabled or Chronically Ill beneficiary to facilitate a life expectancy payout. Sample language with respect to this is included at Appendix G.

The issuance of the 2022 Proposed Regulations and the flexibility afforded thereunder with respect to powers of appointment and modifications of trusts can provide an avenue for the post-mortem modification of trust provisions.

Steve Gorin and Natalie Choate seem to concur that it makes good sense to have this type of clause in a trust agreement, subject to the possibility that the primary beneficiary and his or her descendants may not be best served by having the trust assets not be accessible for such descendants, that in some states such a trust may disqualify the primary beneficiary from receiving public benefits under present or future law, and that the trust may be relatively small or needed to pay for the education and support of the Primary Beneficiary's descendants.

It is therefore suggested that any such "Auto Switch" could be overridden by the actions of a Trust Protector or equivalent individual or entity who would have the power to "toggle off" or taper down, which may be done up through September 30th of the calendar year following the death of the Plan Participant.

Other examples where an "Auto Switch" may be considered are listed below, and by our view will not usually be preferred by a Plan Participant or his or her family, for various reasons.[112] Additionally, these circumstances could warrant a Trust Protector action or use of powers of appointment to effectively change the disposition of IRA/Plan assets following the death of the Plan Participant. Nevertheless, the "Auto Switch" mechanism may relieve the trust protector and fiduciaries who would otherwise have the discretion to make changes from liability exposure that might otherwise occur, as discussed below for each of the enumerated scenarios:

1. <u>A minor child born to the Plan Participant after execution of planning documents</u>.

    A Plan Participant having two adult children may have a trust agreement which provides that, upon his or her death, there would be at least three trusts formed: two separate Accumulation Trusts for adult children, and one Conduit Trust for each minor child designed to qualify for the life expectancy payout method if a third child is born and has not reached age 21 before the death of the Plan Participant.

    Would the Plan Participant have preferred to enable the trustee of the trust for the minor child to take life expectancy distributions which will typically be less than 2% per year until the minor child reaches age 21, with the requirement that all distributions be paid out within ten years thereafter?

    This would seem to make good sense if such a Conduit Trust would be expected to expend all of its assets before the 10-year anniversary of reaching age 21, but if significant assets would have to be paid out to a 28-year-old, this would probably not be preferred. For this reason, many Plan Participants will have a trust agreement that will divide into a separate

[112] LISI Employee Benefits & Retirement Planning Newsletter #721 (March 2, 2020) at http://www.leimbergservices.com, written by Natalie Choate.

Accumulation Trust for each child, regardless of whether one or more of the children are minors upon his or her death.

One thought is to have the "Auto Switch" apply to divide the trust for the minor into one Conduit Trust that would be funded based upon a specific dollar amount that would be expected to be spent before age 28, such as $250,000, with the remaining portion of the minor's share going to an Accumulation Trust that would have to be withdrawn within ten years, but would be preserved under a protective trust system.

Advisors may prefer to have the above-described "Auto Switch" provision apply, and many will want to provide that a trust protector or "inheritance benefit fiduciary" would have the right to override the "Auto Switch."

Alternatively, is it better to simply allow for a trust protector or a plan benefit fiduciary to have that right, exercisable based upon the advice of other family advisors, by September 30th of the calendar year following the year of death of the Plan Participant?

2. Will the significant other become a spouse?

Many clients have long-term relationships without marriage and children by a prior relationship who will be protected by having benefits payable to an Accumulation Trust for the significant other that will allow for the 10-Year Rule to apply and for assets remaining under the trust to pass to the descendants of the Plan Participant after the death of the surviving significant other.

Should the trust provision provide that if the Plan Participant marries the significant other before death, then the Accumulation Trust will become a Conduit Trust to allow for a life expectancy payout. Such a Trust would have to require that all Required Minimum Distributions must be paid directly to the Surviving Spouse, which will cause tax deferral, but could result in much more significant benefits passing to the Surviving Spouse if he or she lives up to or past the normal life expectancy.

As with the minor child, an "Auto Switch" could be used to provide that a certain level of trust assets would be allocated to a Conduit Trust for the Surviving Spouse with remaining assets held under an Accumulation Trust so that the Conduit Trust assets would be used for the health, education, maintenance, and support of the Surviving Spouse with the Accumulation Trust assets being subject to tax in the eleventh year after death, but then retained to be preserved for the descendants of the Plan Participant to the extent that those assets are not needed to support the Surviving Spouse.

In both of the above situations, it seems safest and more thoughtful to allow the trust protector or "inheritance benefit fiduciary" to override the "Auto Switch," but also more complicated.

3. Where the beneficiary is no more than ten years younger than the Plan Participant.There has also been discussion of an "Auto Switch" for a Plan Participant who dies after his or her Required Beginning Date and who leaves an IRA/Plan payable to a trust for a sibling

who is not more than ten years younger than the Plan Participant as an Accumulation Trust to help assure that the assets are properly managed and expended for the sibling.

Should such a trust be separated into a Conduit Trust that can facilitate the lifetime payout for a portion of the funds that seem likely to be expended upon the sibling during their lifetime (such as perhaps $250,000), with excess benefits passing to an Accumulation Trust that will be more likely to be safeguarded for the sibling and the descendants of the sibling?

However, if the beneficiary is of advanced age, then the 10-Year Rule applicable to an Accumulation Trust may actually provide for better financial results due to the tax deferral that the 10-Year Rule affords. This is a great example to illustrate why a Conduit Trust and resulting life expectancy payout might not always be appropriate.

Use of the TEAPOT Trust System

The SECURE Act provides us with less complexity in the long run, but also has increased and accelerated the potential income taxes that are associated with required distributions from IRA/Plans after the death of the IRA owner or retirement plan participant. Specifically, "stretch" payouts over the life expectancies of non-spouse adult beneficiaries who are not disabled, chronically ill, or less than 10 years younger than the deceased Plan Participant have been eliminated. Instead, all assets must be distributed from the IRA/Plan within a usually appreciably shorter timeframe (generally no longer than approximately 10 years after the death of the Plan Participant), and such distributions typically are treated as ordinary income subject to income tax. This can result in a significant departure from the income tax deferral afforded by the "stretch" that was available under prior law.

While qualified advisors can take an educated guess as to how to allocate IRA/Plans among multiple trusts for multiple adult children and their descendants in a tax efficient manner, it is almost certain that such an estimate will miss the mark by a significant degree, given the changes in circumstances, tax law and family objectives, that can change considerably over the course of a decade.

In light of these potential cumbersome challenges, an alternative is for the Plan Participant to leave an IRA/Plan to a single pot trust and to give the trustee thereof the discretionary authority to sprinkle income among the Plan Participant's children and other descendants, while allowing the trustee to conduct an annual strategic review of beneficiaries and their tax situations to determine if and when to make distributions that will carry taxable income out so that the net tax result is optimized. The trust will be drafted as an "Accumulation Trust," meaning that all assets must be distributed from the IRA/Plan no later than December 31st of the 10th year following the year of the Plan Participant's death under the 10-Year Rule, although the trustee is not required to distribute any assets from the trust to the trust beneficiaries.

The pot trust structure allows for tax efficient allocation of IRA/Plan assets between the trust beneficiaries; hence its name- the "Tax Efficient Accumulation POT Trust℠," or the "TEA POT Trust."

When an unmarried Plan Participant dies and has multiple descendants, or the Plan Participant's Surviving Spouse dies and the IRA/Plan had been held under a Conduit Trust (or an Accumulation Trust) for the spouse's lifetime benefit, the typical distribution and division will be for equal shares set aside for each child, or for separate equal trusts to be funded for each child. Normally, these trusts are drafted so that the child can be the trustee or a co-trustee, and the child and his or her descendants can receive distributions as reasonably needed for their health, education, maintenance, or support, although no distributions are required to be made from the trusts. Such trusts should be drafted to qualify as Accumulation Trusts to avoid having the 5-Year Rule apply. While the Treasury Regulations will need to clarify this issue, as described above, it appears to the authors that the At-Least-As-Rapidly Rule will continue to be available to beneficiaries of an IRA/Plan where the Plan Participant has died after reaching his or her Required Beginning Date.

Under the SECURE Act, IRA/Plans that are left to such Accumulation Trusts will be subject to the 10-Year Rule whereby all assets must be distributed from IRA/Plan by December 31st of the 10th calendar year following the Plan Participant's death (or from the Surviving Spouse's death if the IRA/Plan was payable to a Conduit Trust for his or her benefit upon the original Plan Participant's death). Nevertheless, income tax planning opportunities exist to mitigate the effect of the 10-Year Rule.

Most affluent families who have large IRAs also have children who are well-educated and are in the upper income tax brackets, but this is not always the case. For example, an individual with a $900,000 traditional IRA and $3,000,000 of other assets may have one adult child who is in the 40% combined federal and state tax brackets ("Chrys Chamomile"), another adult child in the 25% combined federal and state tax brackets ("Earl Grey"), and a third adult child in the 10% combined federal and state tax brackets ("Chai Green").

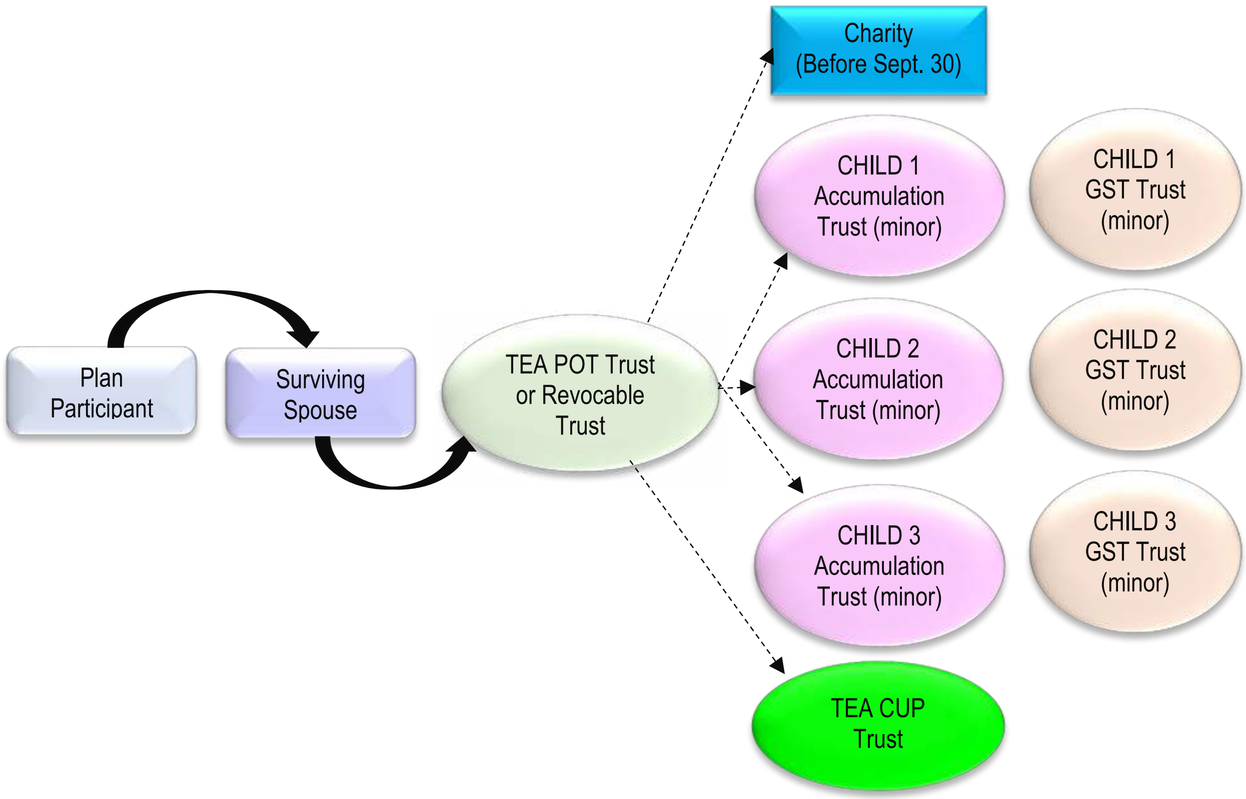
If trusts for the three adult children each receive $300,000 in IRA benefits that have to be paid out within 10 years of the death of the surviving parent, then the taxes that might have to be paid by each respective trust would be $120,000 by Chrys Chamomile ($300,000 x 40%), $75,000 by Earl Grey ($300,000 x 25%), and $30,000 by Chai Green ($300,000 x 10%).

It would make sense to leave the IRA to the trust for Chai Green, and other assets to the trusts for the other children in larger proportions to counterbalance the negative effect of income taxes on the IRA/Plan assets as the required distributions are made, in order to cause greater tax efficiency. However, it will be hard to estimate how much in extra assets to give to the other two children to take into account that Chai Green may have to pay significant income taxes on $900,000, plus growth, coming out of an IRA over 10 years. Additionally, circumstances might change. Chrys Chamomile may become disabled for one or two years and have deductible nursing expenses that would enable him or her to receive $100,000 a year from an IRA tax-free.

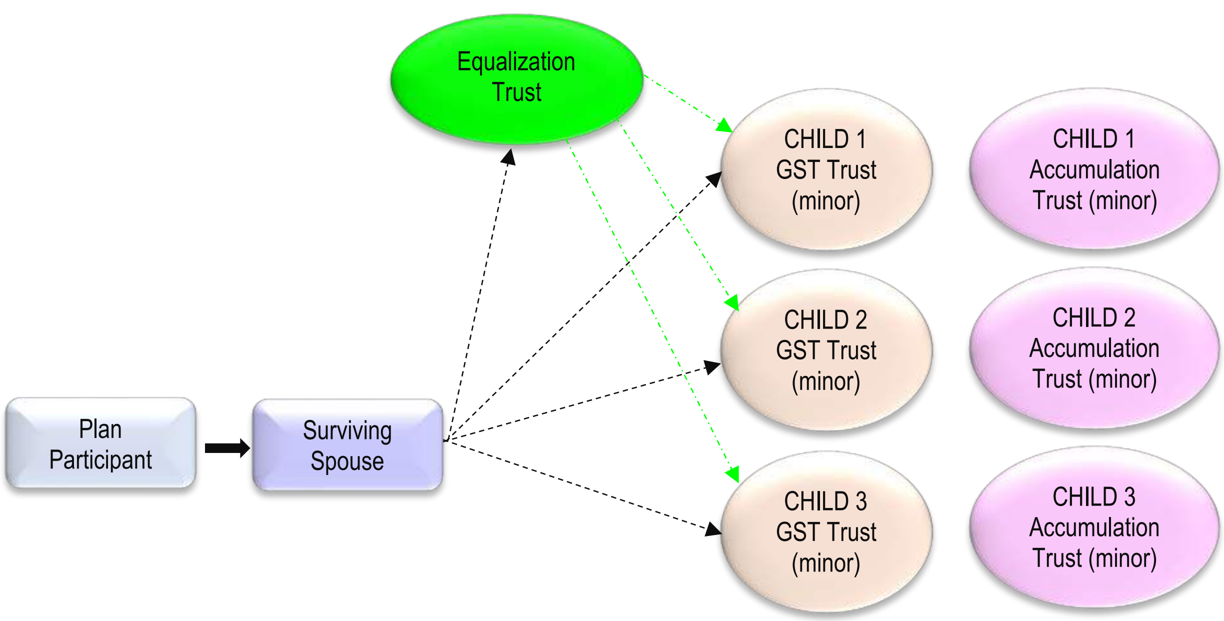
For these reasons, and for this situation, the Twin TEA POT Trust System℠ makes good sense. In the above example, all $900,000 of the IRAs can be made payable to one Accumulation Trust, which can be the beneficiary of one or more IRA/Plans until the tax year after date on which the 10-Year Rule mandates full distribution of all assets from the IRA/Plan. Such time period is referred to as the "Allocation Period" for the purposes of this discussion. During the approximately 10-year period, the trustee of that trust can sprinkle the distributions received among the children and their respective family members as the trustee deems appropriate, taking need and tax brackets into account.

This is why we believe that a “TEA POT Trust” serving solely as the “Stretch Trust” beneficiary of IRA/Plans can provide advantageous income tax results, and that having a non-IRA, non-pension “Equalization Trust” set aside will enable the Trustees to make distributions to or for the benefit of one or more of the descendants or trusts for their benefit to “even things up” during or after the Allocation Period. Sample language for the Twin TEA POT Trust System is included with this Book at Appendix G.

IRA AND PLAN BENEFITS



NON-IRA ASSETS



Obviously, the distributions received by this trust will be expended on some descendants to a greater extent than others. For example, annual payments can be made to Chai Green to make use of the lower brackets each year, as opposed to waiting to give him, or a trust for his benefit, all $900,000 worth, plus growth, in the 10th year.

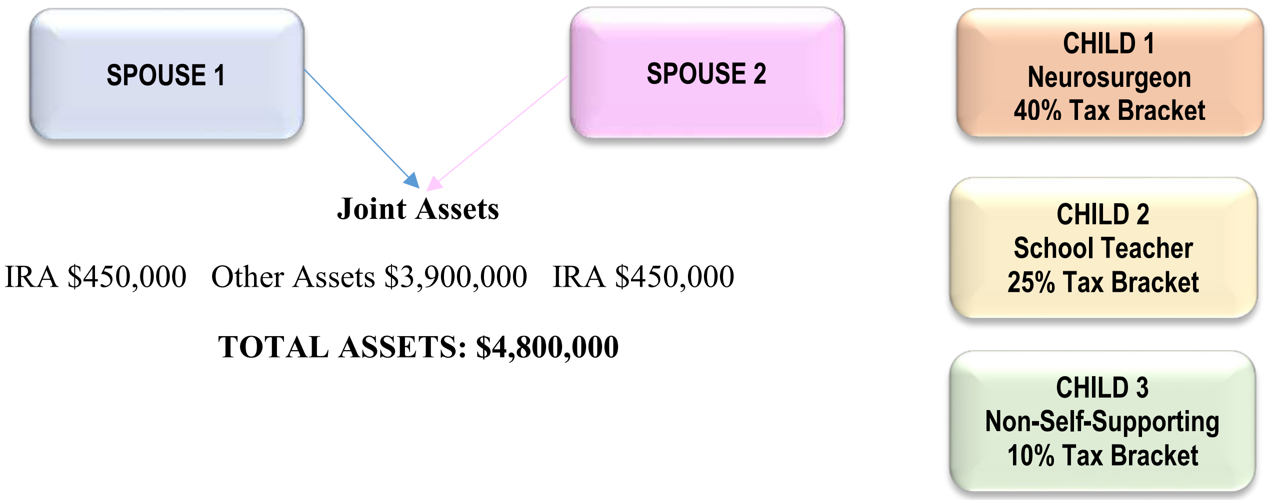
Further, Chrys Chamomile might have a child of her own, Mushroom Brew, who is disabled and has significant deductible medical and personal care expenses. It can make good tax sense for the monies to be spent for low income grandchildren to the extent that they may not be subject to the Kiddie Tax.[113]

In order to keep things fair and equitable, a separate "Equalization Trust" can be established as part of the TEA POT Trust System, which can be held until the expiration of the Allocation Period to provide benefits to the family members who do not receive a "fair share" of the benefit from the TEA POT Trust due to IRA/Plan assets having been allocated to other family members.

In our example, the TEA POT Trust would receive all rights to the $900,000 in IRA accounts, and the Equalization Trust would receive $1,500,000 worth of other assets. This would leave $1,500,000 worth of assets that would be divided into three under the surviving parent's revocable trust shortly after such parent's death, so that the trust for each separate child would receive $500,000 in assets. Over the course of the approximately 10-Year Allocation Period following the surviving parent's death (but no later than the expiration of the Allocation Period), each child's trust will receive the child's one-third share of the total $2,400,000, which can equate to at least $800,000 plus growth (net of taxes).

[113] The Kiddie Tax was also changed by the SECURE Act to cause any investment or unearned income of a child under the age of 19 (or a full-time student between the ages of 19 and 23) to be subject to income tax at the tax brackets of the child's parents, instead of at the tax brackets applicable to complex trusts which applied after the Tax Cuts and Jobs Act of 2017.

SLIDE 1 – TWO PARENTS / THREE ADULT CHILDREN



SLIDE 2 – ONE SPOUSE DIES; SURVIVING SPOUSE ROLLS OVER IRA

SPOUSE 2

IRA	$ 450,000
Rollover IRA	$ 450,000
IRA TOTAL	**$ 900,000**
Other Assets	$3,900,000
TOTAL:	**$4,800,000**

CHILD 1
Neurosurgeon
40% Tax Bracket

CHILD 2
School Teacher
25% Tax Bracket

CHILD 3
Non-Self-Supporting
10% Tax Bracket

SLIDE 3 – SURVIVING SPOUSE DIES (ASSUMING NO GROWTH ON ASSETS)

Slide 3 – Surviving Spouse Dies (For the purpose of this example, we are assuming no growth on assets.)
Inheritance is $900,000 (IRA) +$3,900,000 (Other Assets) = $4,800,000 = $1,600,000 to each child.

TRUST FOR CHILD 1 Neurosurgeon 40% Tax Bracket		TRUST FOR CHILD 2 School Teacher 25% Tax Bracket		TRUST FOR CHILD 3 Non-Self-Supporting 10% Tax Bracket			
1/3 IRA	$300,000	1/3 IRA	$300,000	1/3 IRA	$300,000	$ 900,000	IRA Assets
-40% tax	($120,000)	-25% tax	($ 75,000)	-10% tax	($ 30,000)	($225,000)	Total Taxes due IRS
	$180,000		$225,000		$270,000	$675,000	Balance on IRA (after taxes)
Other Assets	$1,300,000	Other Assets	$1,300,000	Other Assets	$1,300,000	$3,900,000	Total Other Assets
Child 1 Total:	$1,480,000	Child 2 Total:	$1,525,000	Child 3 Total:	$1,570,000	$4,575,000	IRA TOTAL

DISADVANTAGES TO THE ABOVE ARRANGEMENT

Disadvantages to the above arrangement:

1. Paying tax on IRA distributions at higher rates than need to apply, even if distributions are made from IRA over a number of years so as to reduce the marginal tax rate applicable to such distributions.

2. The IRA monies could be allocated more or less as opposed to equally between the children's trusts, but they may disagree on what adjustments should be made to facilitate this.

3. Beneficiaries may spend their trust assets too quickly.

4. Even if the children engage in using IRA withdrawals in the most tax efficient manner, it will be cumbersome, and there will be a high probability of errors or simply ignoring savings that could occur.

5. It is not flexible because there may be changes. For example: Child 1 may have an autistic stepchild who could easily receive money tax-free from an IRA.

6. Each child's trust needs to meet the definition of an Accumulation Trust, and each child has to have a separate Accumulation Trust.

SLIDE 4 –
IMPLEMENT TWIN TEA POT TRUST SYSTEM AFTER DEATH OF SURVIVING SPOUSE

Slide 4 – Implement Twin TEA POT Trust System After Death of Surviving Spouse to maximize income tax savings

Equalization Trust

Assets $1,400,000

Can review the TEA POT distributions for the first 10 years and distribute "makeup payments" to beneficiaries or trusts to take TEA POT payments into account.

If TEA POT Trust makes distributions every other year, then Equalization Trust can do the same.

"TEA POT" Trust

Assets $ 900,000

First 10 Years After Death:

Trustees can hire advisors to determine how to reduce income taxes and defer for up to 10 years by making payments to or for the lowest tax bracket beneficiaries and those who may have significant expenses and deductions.

NOTE: Charitable Dispositions might be made from "Equalization Trust" at the request of one or more beneficiaries before September 30th of the calendar year following the Plan Participant's death.

TRUST FOR CHILD 1
Neurosurgeon
40% Tax Bracket

Non-IRA Assets $833,333

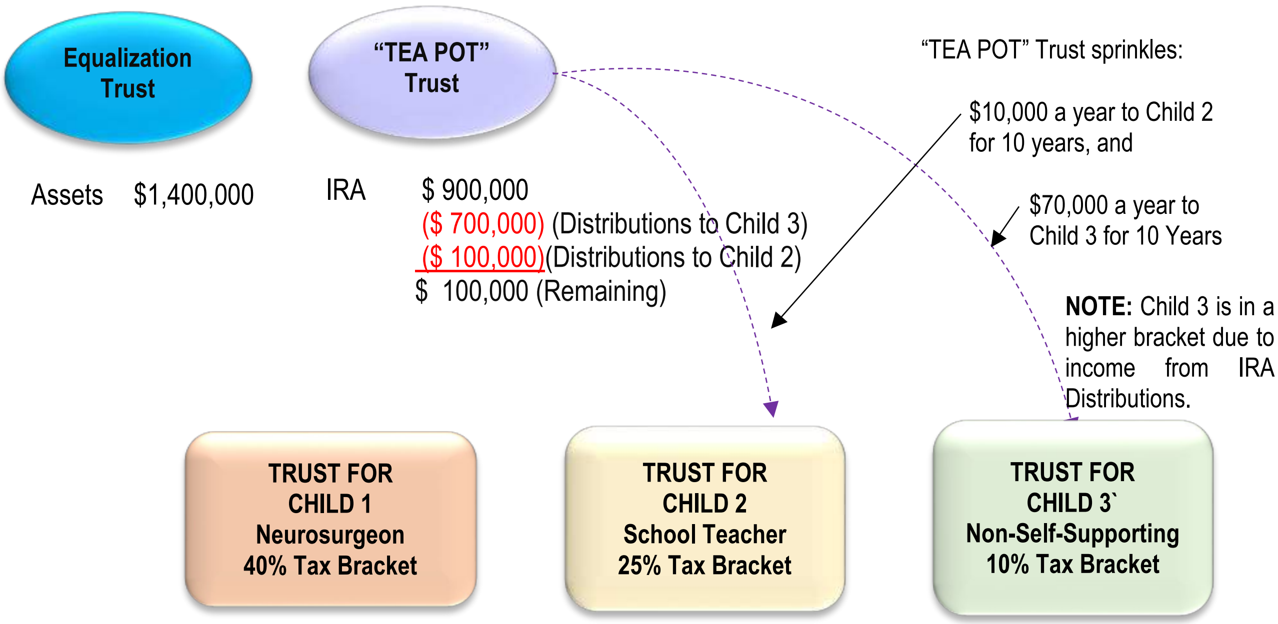
TRUST FOR CHILD 2
School Teacher
25% Tax Bracket

Non-IRA Assets $833,333

TRUST FOR CHILD 3
Non-Self-Supporting
10% Tax Bracket

Non-IRA Assets $833,333

SLIDE 5 – IRA DISTRIBUTIONS FIRST 10 YEARS AFTER SECOND DEATH

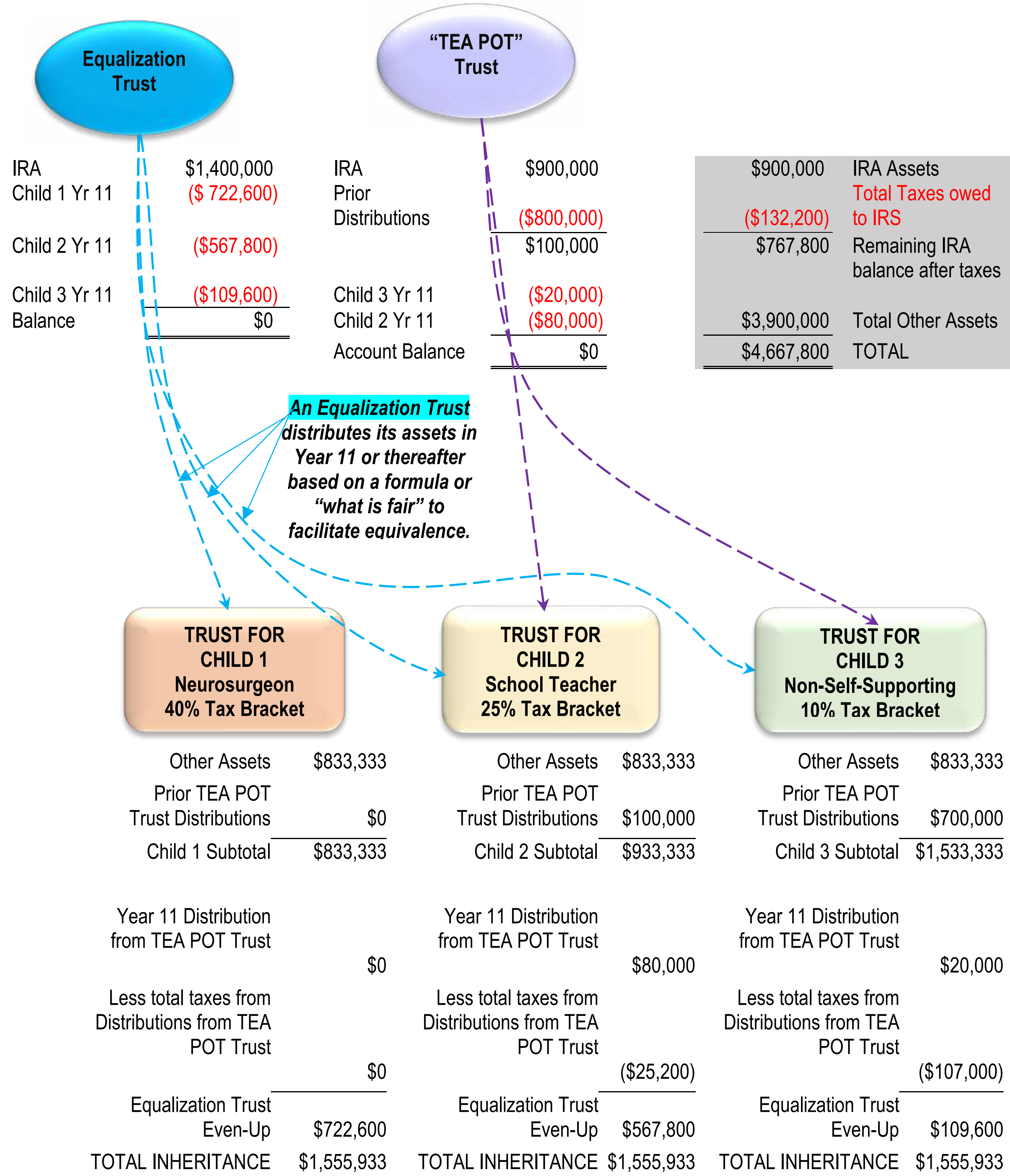


		Distributions from TEA POT Trust	$ 100,000	Distributions from TEA POT Trust	$ 700,000
		Taxes on Distributions	($ 25,000)	Taxes on Distributions	($ 105,000)
Other Assets	$ 833,333*	Other Assets	$ 833,333*	Other Assets	$833,333*
Child 1 Total:	$ 833,333	Child 2 Total:	$ 908,333	Child 3 Total:	$1,428,333

*(To be used for health, education, maintenance, and support)

(Above is during first 10 years – before even-up from Equalization Trust)

SLIDE 6 – EQUALIZATION TRUST EVEN-UP IN YEAR 11



Note: For purposes of illustrating the mechanics of the structure, we have not assumed any appreciation or income earned on any assets including growth and income associated with the assets held under the above trusts which will slowly compound the effects of the TEA POT Trust System.

ADVANTAGES TO THE ABOVE ARRANGEMENT

Advantages to the above arrangement:

1. The IRA income will be taxed at much lower brackets.

2. Each child can be treated equally, if the parents want. Alternatively, if the parents want to favor children who are in lower tax brackets, not including a time value of money makeup provision in the non-TEA POT Trust, which actually indirectly helps the lower bracket children without such intention being expressed in the document.

3. The IRA tax planning can be only in one trust, so you do not have to have three separate trusts that meet the definitions of an Accumulation Trust. For example, the Accumulation Trust cannot benefit charity or any entity other than the child.

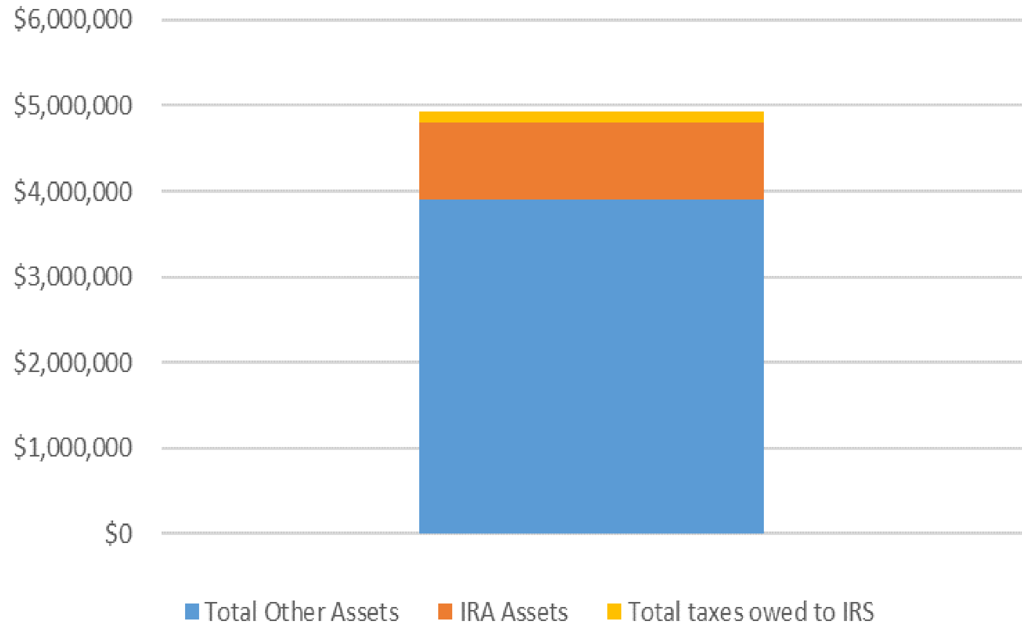
4. This forces the tax family to do tax planning every year – because the whole nature of it, they have to meet with their lawyer or their CPA every year to do it.

5. Children might be inclined to be more financially prudent due to the potential for a child's share being reduced in Year 11.

COMPARISON OF RESULTS WITH AND WITHOUT TEA POT TRUST SYSTEM

Results with TEA POT Trust System		Results Without TEA POT Trust System	
IRA Assets	$ 900,000.00	IRA Assets	$ 900,000.00
Total taxes owed to IRS	($132,200.00)	Total taxes owed to IRS	($225,000.00)
Remaining IRA balance after taxes	$ 767,800.00	Remaining IRA balance after taxes	$ 675,000.00
Total Other Assets	$3,900,000.00	Total Other Assets	$3,900,000.00
TOTAL	$4,667,800.00	TOTAL	$4,575,000.00

RESULTS WITH TEA POT TRUST SYSTEM



RESULTS WITHOUT TEA POT TRUST SYSTEM

A competent CPA who understands income taxes for individuals and trusts can be retained by the trustee of the TEA POT Trust and can advise each year on whether to take a distribution and how to allocate the distribution to most effectively reduce income tax and enhance the inheritance of all beneficiaries.

The TEA POT Trust and the Equalization Trust can be managed by all of the children, along with a professional or corporate trustee, if desired, and someone from outside of the family, like a long-term lawyer, CPA, or other advisor or close friend can serve to act as the "tie-breaker" in order to help determine how the Equalization Trust is distributed. Alternatively, a CPA firm could be named and given the task to determine what the after-tax impact of the TEA POT Trust has been, and to calculate how much of the Equalization Trust should be distributed to the trusts for the separate children in order to facilitate after-tax sharing in the most equitable manner.

Most tax and estate planners are well aware that a separately taxed "complex trust" measures its taxable income in a manner very similar to what applies to individuals, but that distributions made during a tax year, as well as distributions made within 65 days of the end of the tax year that the trustee elects to have considered as having been distributed in the previous year.

As discussed below, there is a question of whether the IRS will consider the TEA POT Trust and the Equalization Trust to be considered as one trust for federal income tax purposes.

Because of this, it will be safest to not make distributions from the Equalization Trust in the same calendar year that distributions are made from the TEA POT Trust, so that the IRS does not treat the income as coming pro rata from each trust to the recipient beneficiaries. Some families will distribute from the TEA POT only for the first ten years, and then from the Equalization Trust, while others may alternate years – Year 1 from the TEA POT Trust, Year 2 from the Equalization Trust, etc.

With reference to if and when two or more trusts will be considered to be a single trust, under Internal Revenue Code Section 643(f) and Treasury Regulation Section 1.643(f), two or more trusts will be treated as one trust if they have all three of the following:

(1) substantially the same grantor, with married couples being considered as one grantor, even if they each separately establish a separate trust;

(2) substantially the same primary beneficiaries, and

(3) a principal purpose of such trust is the avoidance of income tax. One question is whether the deferral of income tax by use of an Accumulation Trust is considered to be the "avoidance of income tax." It seems at least arguable that the deferral of income tax is different than avoidance.

Under the prior law, "shadow trusts" have been commonly used for the purpose of being the beneficiary of IRA/Plans after the death of the Plan Participant, so that the rules and limitations required to qualify the trust as a "See-Through Trust," are complied with. This may provide sufficient justification to establish a multiple trust arrangement for reasons other than to avoid income tax. Further, it may be sufficient if each trust has different provisions regarding the distribution of income or principal, and one trust provides for the possibility of distributions being made to beneficiaries who are not beneficiaries of the other trust. For example, the Equalization Trust could permit the trustee thereof to make distributions of non-IRA Plan assets to charitable organizations.

A separate TEA CUP Trust could be established from the IRA accounts otherwise intended for the TEA POT Trust if there is a chronically ill or disabled beneficiary who is intended to receive IRA/Plan assets. The TEA CUP Trust can be structured as an Accumulation Trust for the benefit of such chronically ill or disabled beneficiary, and the TEA CUP Trust should be entitled to Stretch IRA treatment with respect to Required Minimum Distributions payable over the lifetime of the chronically ill or disabled beneficiary. This is because a chronically ill or disabled beneficiary is an Eligible Designated Beneficiary to which the Life Expectancy Rule applies, and a special exception unique to chronically ill or disabled beneficiaries allows for the Life Expectancy Rule to apply even if the IRA/Plan is made payable to an Accumulation Trust for the benefit of the chronically ill or disabled beneficiary and such separate Accumulation Trust is divided from a larger trust after the death of the Plan Participant.

It is noteworthy that an Accumulation Trust established for a minor must be directly funded to qualify for the use of the minor's life expectancy through age 21, so it does not appear that a TEA POT Trust can share its assets to fund a TEA CUP Trust under the new law.

In addition, the family may have charitable intentions, and the TEA POT Trust can allow the trustee to make distributions from the IRA/Plans accounts directly to charity provided that no such distributions may be made to any charity or other non-individual after September 30 of the of the calendar year following the year of the death of the Plan Participant. The September 30 deadline serves to help assure that the Trust will qualify as an Accumulation Trust, as only individuals can be beneficiaries of an Accumulation Trust after such September 30. This means that the family may huddle shortly after the Plan Participant's death to determine how much or what to give to charity, and which beneficiaries will have their inheritance trusts reduced to take this into consideration.

While we recommend that neither of the TEA POT Trusts have any disposition to charity after the September 30 of the year following death date, it seems that the tax law will permit the Equalization Trust to invest its assets in an entity taxed as a partnership, and to receive ownership in the partnership in exchange for such investment. The partnership can make charitable contributions and can receive an income tax charitable deduction that is passed through to its partners (including the Equalization Trust) on Forms K-1. It might be possible for the TEA POT Trust to be a partner in the partnership as well, but the IRS may argue that the charitable recipients of the partnership's charitable contributions are considered to be beneficiaries of the Trust, which would cause detrimental effects to the TEA POT Trust's ability to qualify as an Accumulation Trust.

The TEA POT Trust has other advantages besides tax savings and flexibility, namely:

1. The TEA POT Trust will relieve the children and their respective trustees from having to work with smaller ($300,000 each in our example) IRA stretch trusts that will need to be separate and apart from their other lifetime benefit trusts in order to

have the 10-Year Rule period apply, and to avoid the expenses and possible mistakes associated with the administration and maintenance thereof.

2. The TEA POT Trust keeps the children together with respect to the management and distribution thereof, as opposed to each child going their own separate way from an investment decision-making, management and interpersonal standpoint. Further, the Trust can require that each child attend an annual meeting, and that competent advisors be hired and used.

   The most adept and conscientious child or children will hopefully set a good example and "rub off" on the less adept and less attentive child or children, which may influence everyone to do a better job in being a trustee or co-trustee for their own trusts. Additionally, an advantage to not having separate trusts is that one child may have little or no appreciation for the need of staying in touch and requesting assistance from competent tax and legal advisors.

3. As stated above, the TEA POT Trust can provide the creditor protection and asset preservation benefits afforded by a spendthrift trust that does not require compulsory distributions therefrom. This is perhaps the most significant advantage of the TEA POT Trust relative to the IRA/Plan being left directly to a child or to a Conduit Trust for the child.

4. Having the children receive additional distributions after the Allocation Period can help assure that the trusts for the children and subsequent generations are not inadvertently exhausted.

5. The TEA POT Trust will be more flexible, if there are law changes in the future, because of the special language that can be provided in the trust agreement to facilitate this.'

A Refresher on Distributable Net Income and IRA/Plan Benefits Payable to Trusts

Internal Revenue Code Section 661 and 662 provide that a trust will receive a distribution deduction to the extent that distributions are made, but not in excess of Distributable Net Income.

Internal Revenue Code Section 643(a) defines Distributable Net Income as the taxable income of the trust with the following modifications:

1. No personal exemption ($300 for simple trust/ $100 for complex trusts).

2. Capital gain and losses are excluded to the extent such gains and losses are allocated to principal unless they are (a) "paid, credited, or required to be distributed to any beneficiary during the taxable year" or (b) "paid, permanently set aside, or to be used" for charity.

3. Internal Revenue Code Section 1202 is not taken into account.

4. Tax-Exempt interest is included net of any deductions attributable to such interest.

Distributable Net Income is allocated based upon a two-tier system:

1. The first tier consists of distributions of fiduciary accounting income that are required to be distributed in the current year by the Trust Agreement (e.g. "the Trustee shall distribute all income annually to my son Jim"). First tier distributions carry out Distributable Net Income first pro rata to amounts received by each recipient of such required payments.

2. The second tier consists of any other amount of property paid or credited, or required to be distributed, during the tax year (e.g. "the Trustee may distribute so much of the income and/or principal of the Trust as the Trustee shall deem appropriate to my son Jim"). Second tier distributions carry out any remaining Distributable Net Income after Distributable Net Income is allocated to first tier distributions pro rata to amounts received by each recipient of such payment.

EXAMPLE:

A Trust has $25,000 of Fiduciary Accounting Income and provides that all income must be distributed to Adam. The Trust additionally provides that the trustee has the discretion to distribute additional amounts as needed for the health, education, maintenance and support of Adam and Bob. The Trust has $100,000 of taxable income and the trustee distributes $50,000 to Adam ($25,000 of income and $25,000 of principal) and $25,000 to Bob.

Since $25,000 of income is required to be distributed to Adam (a Tier 1 distribution) $25,000 of Distributable Net Income is allocated to Adam first. The remaining $50,000 of income is allocated equally between Adam and Bob (a Tier 2 distribution) so that Adam receives an additional $25,000 of Distributable Net Income (total of $50,000) and Bob receives $25,000 of Distributable Net Income.

The remaining $25,000 of taxable income is taxed to the trust since it was not distributed out to the beneficiaries.

Income from the receipt of IRA/Plan benefits by the trust is included in taxable income and is therefore included in the Distributable Net Income that can be passed out to the beneficiaries. However, under the Principal and Income Act of most states, IRA/Plan distributions to a trust are treated as principal for fiduciary accounting purposes.

As a result, if the trust agreement only provides for distributions of fiduciary accounting income to a beneficiary, then income recognized by the trust upon the receipt of distributions from an IRA/Plan cannot be passed out of the trust in the year when taxable income exceeds fiduciary

accounting income, unless the trust specifically provides for the income received from IRA/Plans to be allocated to income.

When using the TEAPOT Trust System with the intent to allocate IRA income to low income beneficiaries, care must be taken to properly draft and administer the trust to allow for this allocation to occur. For example, a mandatory distribution of income to a high-income beneficiary would result in a Tier 1 distribution and the automatic allocation of Distributable Net Income to such beneficiary. Additionally, distributions cannot be made to multiple beneficiaries in different tax brackets since Distributable Net Income is allocated on a pro rata basis unless separate shares are created to specifically allocate IRA assets to the share of the low-income beneficiary.

Possible Use of Section 678 Trusts

Normally, an Accumulation Trust will be taxed as a Complex Trust, so that income held under the trust and not distributed will be taxed at the highest bracket to the extent exceeding $13,450 in 2022.

In addition, distributions made to high income taxpayers will be taxed at their brackets, and the Medicare tax will also apply to income retained by a Complex Trust which exceeds $13,450 in 2022, or for individual taxpayers who have more than $200,000 of taxable income if single, or $125,000 if married filing separately.

An Accumulation Trust may alternatively be taxed as if all of its income was actually received by an individual beneficiary, if Internal Revenue Code Section 678 applies. The authors are not aware of any reason that a Section 678 Trust cannot qualify as an Accumulation Trusts, although some authors have indicated that they are not sure whether this will be the case, so it seems best to draft to allow Trustees to convert Accumulation Trusts that would be considered as Complex Trusts for income tax purposes into Section 678 Trusts after the death of the Plan Participant, based upon the status of the law and decision-making by or for a family member after the death of a Plan Participant, when the tax law may be more firmly established with respect to whether this is a viable option.

Under Internal Revenue Code Section 678, an individual will be considered to be the owner of all income and deductions of a trust, if that individual has had or has "partially released" the right to income or corpus of the trust, and the trust is not considered for income tax purposes to be owned by its grantor.

A number of Private Letter Rulings have indicated that an individual who has the right to withdraw all trust assets and completely releases such right will be considered to be the owner of the trust for income tax purposes, but it seems safer to have the individual release substantially all, but not 100% of the withdrawal right in order to be sure that Section 678 will apply.

In order to have the flexibility to create one or more Section 678 Trusts that are IRA or pension plan beneficiaries after the death of the Plan Participant, the trustee who is not the "678 beneficiary" or an Independent Fiduciary can have the power under the Trust Agreement to divide the trust into two or more separate trusts, and to provide the Section 678 beneficiary with the right to withdraw income or corpus from one or more of such trusts, in a manner that permits the Section 678 beneficiary to partially release it.

EXAMPLE:

The Section 678 beneficiary may release 95% of the power, and remain able to withdraw up to 5% of the trust principal and income each year, and then all income required by the trust, as well as amounts that are distributed to the Section 678 beneficiary and higher bracket beneficiaries will be taxed at the Section 678 beneficiary's lower bracket on his or her Form 1040 income tax return, regardless of whether income or principal is distributed to such beneficiary.

Creditors of the Section 678 beneficiary will be able to reach trust assets, unless the trust is sitused in an asset protection jurisdiction, assuming that the law of the asset protection jurisdiction will be controlling.

If and when it is desired to not have creditors of the Section 678 beneficiary be able to reach into the trust, or to not have the trust treated as a Section 678 Trust, it will be possible to have the trustee or an individual holding a Power of Appointment under the trust document to direct the trust assets to one or more of the other beneficiaries, or a trust for one or more of the other beneficiaries.

For further discussion of Section 678 Trusts, see LISI Estate Planning Newsletter #2577 (September 5, 2017) at http://www.leimbergservices.com, which is available from him at Edwin.Morrow@usbank.com upon request.

In addition to the above, other alternatives exist under these planning scenarios, that are worthy of consideration:

1. When an IRA or Pension Account is Payable to a Properly Drafted Charitable Remainder Trust.

   The taxation and advantage of using a charitable remainder trust as the beneficiary of an IRA/Plan is not specifically provided for under the SECURE Act, but the tax law is very clear that an IRA/Plan passing by beneficiary designation to a properly drafted and administered charitable remainder trust will not cause imposition of income tax on such distributions unless or until distributions are made by the charitable remainder trust. As discussed in Chapter 5, such distributions can be paid out over the life expectancy of the individual charitable remainder trust beneficiary or over a fixed period of years not to exceed 20 years.

   It is noteworthy that a fixed term payout charitable remainder trust, which may make payments over 20 years, can have the annual distributions "sprayed" out in varying amounts among multiple beneficiaries or entities for such beneficiaries, while a lifetime payout charitable remainder trust must distribute the monies directly to the applicable beneficiary, or in equal shares to multiple beneficiaries. Payments coming from a lifetime payout charitable reminder trust must go directly to each individual beneficiary, with the exception of having certain trusts receive distributions for a disabled beneficiary.

A charitable remainder trust does not pay income taxes for the items of income it holds onto; income tax liability is only incurred if income is distributed to the non-charitable beneficiary. Thus, the IRA/Plan distribution amounts can be contributed to a charitable remainder trust over the 10-year required distribution period, and the charitable remainder trust will not have to pay income taxes on the assets that it continues to hold. This allows the charitable remainder trust to earn and accumulate income without paying taxes on such income until the distributions are made to the lifetime non-charitable beneficiary.

At least 10% of the charitable remainder trust assets must be projected to go to the ultimate charitable beneficiary based upon the life expectancy tables as described under Section 7520. These are referred to as the 2000 CM Mortality Tables, which likely understate the life expectancy for the non-charitable beneficiary because these numbers were compiled based upon data from the year 2000. As medical technology continues to improve, the life expectancy of individuals, especially for those who have the means to consider a charitable remainder trust for their IRA/Plan, will hopefully continue to rise. Thus, it is likely that the charitable remainder trust will continue to pay the non-charitable lifetime beneficiary for a period of time that is in excess of what the life expectancy tables would project, resulting in more value going to the non-charitable beneficiary and less going to the charity.

This plan can work out very well for Plan Participants who are somewhat charitable minded and would like their beneficiaries to receive their IRA/Plans over an extended period of time to avoid and delay income tax liability.

It may work well to create a 20-year charitable remainder trust for a spouse that has less than a 20-year life expectancy in order to provide greater benefits for the original plan owner's children. In such an event, the charitable remainder trust can continue to grow assets tax free and make distributions to the original plan owner's children after the spouse passes.

Otherwise, the payout percentages to a Surviving Spouse who is age 80 would be 5.35% that year, increasing each year thereafter, whereas under a 20 year charitable remainder trust the percentage would be 4.902% per year for 20 years, with the remainder passing to a family foundation that can be managed by and pay reasonable compensation to family members. The charitable remainder trust numbers assume the use of the January 2020 Section 7520 rate of 2.0%.

Taxpayers need to consider a number of factors when determining if a charitable remainder trust would achieve their desired estate planning goals and taxpayers should consult a tax attorney to help them navigate the available options.

For a more detailed discussion of charitable remainder trusts, and charitable planning relating to IRA/Plans, please see Chapter 5 of this Book.

2. Spousal Accumulation Agreements.

An alternative to an Accumulation Trust or Conduit Trust may be a legally binding agreement between spouses, with children and other descendants as third party beneficiaries, which requires the Surviving Spouse to only withdraw the Required Minimum Distribution amounts each year from a rollover IRA, to invest based upon whatever guidelines and limitations may be set forth in the Agreement, and to provide for the IRA/Plan to be inherited by the descendants of the first dying spouse, or trusts for their benefit, in the manner set forth under the Agreement.

This should preserve the Surviving Spouse's ability to take distributions out in the most tax efficient manner, to have state law creditor protection for the IRA/Plan and distributions from the IRA/Plan to the extent applicable, and to follow the wishes of the first dying spouse, while having the benefit of use of the IRA/Plan to the extent permitted under the Agreement, and such other assets, whether inherited in trust or outright, as may be left for the Surviving Spouse.

One question is how the descendants of the first dying spouse or other beneficiaries will enforce such an agreement if they cannot reach the IRA/Plan or other assets that are creditor exempt if they get a judgment against the Surviving Spouse. Such agreement will nevertheless be enforceable against other assets that the Surviving Spouse might not want to lose by violating the agreement, or may provide that the spouse is considered to be holding the IRA/Plan as "trustee" of a constructive trust for state law remedy purposes, so that an equitable lien might be given to the descendants if the agreement is violated. Also, equitable relief may be permitted under the agreement, if enforceable under state law.

In states that have complete creditor protection for IRA/Plans and payments made from IRA/Plans, the spouse will be safer under an Accumulation Trust than under a Conduit Trust, where distributions received from the trustee will not be protected from creditors. In most states that protect IRA/Plans, payments received, as well as other creditor exempt assets purchased with payments received are completely protected from creditors.

At one time, it was unclear whether IRA/Plans would be protected under the federal exemption provisions of the bankruptcy code because IRA/Plans are not ERISA plans. The United States Supreme Court provided that federal bankruptcy law will not protect inherited IRAs for those residing in states that do not have state exemption statutes for IRAs through its decision in the *Clark v. Rameker* case.[114]

The following discussion reiterates much of what is provided in Chapter 6 on creditor protection for IRA and pension accounts.

For individuals who live in states that do not provide creditor protection for IRA/Plan accounts, such protection will still apply if the individual files bankruptcy

[114] *Clark v. Rameker*, 573 U.S. 122 (2014).

to the extent that the balance of the IRA/Plan does not exceed $1,362,800 as of 2020, for traditional IRAs and Roth IRAs funded by the IRA owner. Some states provided for added levels of creditor protection for IRA/Plans, such as Florida, which does not allow a judgment creditor to recovery against IRA/Plan or inherited IRA accounts.

Pursuant to Bankruptcy Code Section 522(n), when the Federal exemptions apply, assets held in traditional IRA and Roth accounts are exempt from creditors and thus not part of the bankruptcy estate; however, assets attributable to amounts rolled over from the IRA/Plan are not exempt and will not be included in the $1,362,800 limit. For this reason, clients are well advised not to mix contributory IRA/Plans with other IRA/Plans that come from spousal rollovers or pension plans so that it is clear which account the $1,362,800 limitation applies to.

The IRA/Plan will no longer receive protection from creditors in the event that the Plan Participant enters into a prohibited transaction with the IRA/Plan or does not comply with the IRA/Plan rules. The case, *In re Yerian*,[115] provides an example of this where a taxpayer engaged in self-dealing transactions prohibited by the IRA/Plan's governing documents by titling IRA/Plan -owned cars into his own and his wife's name. He also purchased a condo with IRA/Plan funds. The Florida court held that these actions resulted in loss of the creditor protection status of the IRA/Plan.

Prohibited transactions include the following:

i. The provision of goods, facilities, or services between a plan and a disqualified person;

ii. Lending money from a plan to a disqualified person;

iii. The sale, exchange, or lease of any property between a disqualified person and a plan; and

iv. Transferring assets from the plan to a disqualified person.

As the result of the above, many planners should add the IRA/Plan Spousal Accumulation Agreement to their estate planning repertoire, assuming that there will not be a concern that the IRS will see the arrangement as a pseudo Accumulation Trust and attempt to require a distribution at the end of the 10th year.

The Agreement can require the appointment of a fiduciary to ascertain whether the 10-Year Rule would apply in such arrangement and might require a distribution in the 10th year if this appears to be the case, which the authors believe would be unlikely.

[115] *Yerian v. Webber (In re Yerian)*, 927 F.3d 1223, 1225 (11th Cir. 2019).

3. The IRA Trust.

An IRA Trust is a trust that can be the beneficiary of an IRA/Plan and will have a trust company as the trustee. An IRA Trust can use the Conduit or Accumulation Trust rules as selected by the trustee, without having to have language in the Trust Agreement that is otherwise required for a Conduit Trust or an Accumulation Trust, and the trust company can select which alternative to use on or before September 30th of the calendar year following the death of the Plan Participant.

4. Disclaimer Planning.

While the Distribution Rules require that an IRA/Plan be payable in a particular manner that is irrevocable upon the death of the Plan Participant, well designed estate plans can allow the surviving family members and trustees to elect between a number of different alternatives by use of proper disclaimer planning.

On the other hand, disclaimer claiming can also be useful. For example, many clients will name the Surviving Spouse as the beneficiary of an IRA/Plan, with the alternate beneficiary being a Conduit Trust under provisions that would allow the trustee of the Conduit Trust to amend the trust to become an Accumulation Trust, or to disclaim the distribution with the alternate beneficiary being an Accumulation Trust. The trustee of the Accumulation Trust may have the right to disclaim the benefit so that it would pass to trusts for the descendants, and the trustees of the trusts for the descendants may have the right to disclaim the benefit to go to a public charity or a private foundation that might be formed by the family, and managed by family members who may receive reasonable compensation for charitable activities, and maintaining the investments of the foundation.

Please note that disclaimer planning will only work if the alternate beneficiary that eventually does not disclaim is an appropriate individual, individuals, a Conduit Trust, or an Accumulation Trust, and that beneficiary designations cannot be changed after the death of the Plan Participant, and if the disclaimer is a “Qualified Disclaimer” under Internal Revenue Code Section 2518 that is made within nine months of the Plan Participant’s death.

SCENARIO L – IRA TO CHILD A – ALLOWS DISCLAIMER TO CHARITY[116]

If Child A disclaims, no tax is triggered.

1. Charity cannot be private foundation over which the disclaimant is trustee or manager with power to direct the foundation's assets.

2. Disclaimants may recuse themselves from decision making power via a "Chinese Wall" provision to avoid disclaimer being deemed invalid.

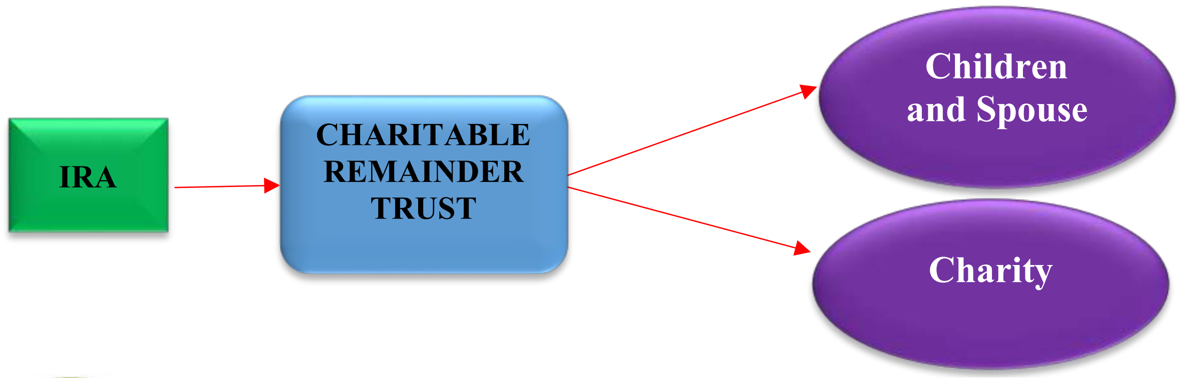
3. Disclaimants should consider recusing themselves from decisions over donor-advised funds. One PLR has held that a disclaimer in favor of donor-advised funds does render disclaimer invalid due to the fact that the disclaimant is merely an advisor and cannot "direct" distributions. PLR 200518012.

<u>Possible clause to facilitate the above:</u>

"I intend to have $500,000 be paid to A Museum, located in Any City, Florida, provided that it is a 501(c)(3) organization and have been advised that it would be preferable to fund such devise from my IRA. I have therefore named my son Eric as beneficiary of my IRA B, with such charity being the alternate beneficiary. I request that my son determine whether it works best for federal income tax and estate tax planning purposes to disclaim such devise so that the IRA can pass directly to the Museum or to receive some or all of such devise as an inherited IRA and to make contributions to the Museum individually to receive income tax deductions. I recognize that this provision is not binding upon my son."

[116] Scenario L is also included in this Book on page 137.

SCENARIO M – IRA GOES TO CHARITABLE REMAINDER TRUST[117]



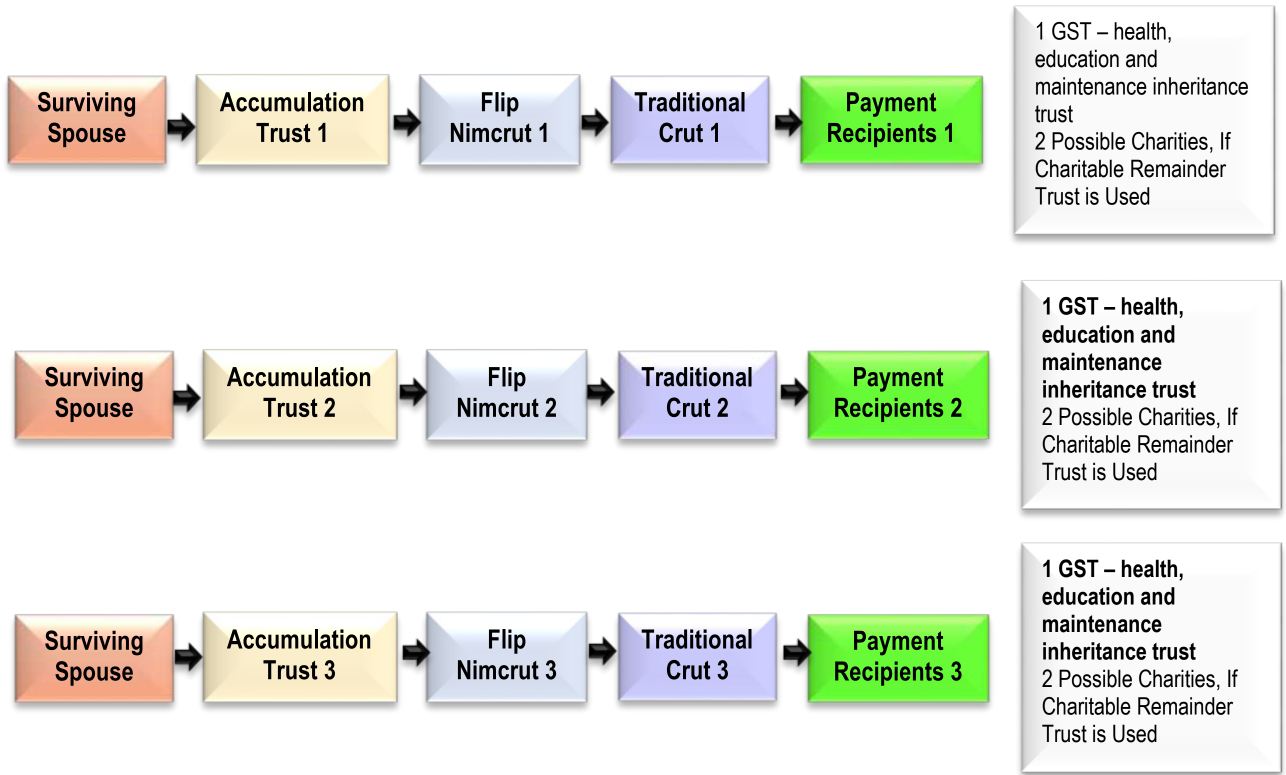
Payable to Charitable Remainder Trust which will make lifetime payments to my children and spouse, remainder to charity.

No Income Tax paid on benefits payable to Charitable Remainder Trust.

Distributions to Individuals will carry out taxable income on a"worst first" basis.

[117] Scenario M is also included in this Book on page 138.

SCENARIO O – POSSIBLE CASCADING DISCLAIMERS FOR CHARITABLE PLANNING



5. <u>Outright Distributions to Charity</u>.

Charitable planning is covered extensively in Chapter 5, but the general rule with respect to direct distributions to a 501(c)(3) organization named as the beneficiary of an IRA/Plan is that no tax will be paid on the IRA or plan assets that are delivered to charity after the death of the Plan Participant.

In addition, an estate or trust that receives an IRA/Plan distribution after the death of the Plan Participant, and properly authorized under the trust document or Last Will and Testament to make payment to charity will have the ability to deduct such payment, and the charity will not have to pay tax on receipt thereof, if the proper rules are followed.

A good many taxpayers who are charitably inclined will take a look at these new rules and simply decide that it is better to have IRA/Plans be payable directly to charity than to have them be subject to a 10-Year Rule. As many clients get older and wealthier, and as their children also get older and become more and more self-sufficient, they may determine that there is less need for family support (and paying large taxes to the IRS), and more room to make charitable donations.

An IRA/Plan can be payable to a Revocable Trust, with the trustee being required or having discretion to make distributions to charity. This will carry all of the income from the IRA or pension account withdrawal to the charity in the amount that the charity receives. If the estate would otherwise be subject to federal estate tax, this is a double win.

It is important to note that a pecuniary (fixed dollar amount) devise from an estate or trust to charity may trigger income tax on "*Kenan*" gain, if one or more appreciated assets are transferred to charity to satisfy a fixed dollar amount disposition, and there is extensive discussion regarding payments from estates and trusts to charity in Chapter 5.

A SECURE ACT CHECKLIST

Now that we have covered the rules that will apply Post SECURE Act, the following is a checklist of items that can be used for client interactions:

1. Notify that Required Beginning Date has been moved from 70½ to 72.

2. Reminder that a 70½-year-old can move up to $100,000 per year directly from taxable IRA/Plan to a public charity to avoid 50% of AGI limitation.

3. Notify that 529 Plan monies can now be used to pay up to $10,000 in student loans for the 529 Plan beneficiary and each sibling - but only up to $10,000 per person.

4. Consider income tax planning for children and young adults under the new Kiddie Tax where the parents of the child are not in the highest tax bracket.

5. Notify that IRAs can now be used to pay up to $5,000 for childbirth/adoption costs ($10,000 if both parents have IRAs and wish to withdraw).

6. While in contact, on other fronts:

    a. Notify that under the Powell and Strangi cases, all assets held under a family limited partnership or LLC may be subject to estate tax/stepped-up basis - as if still owned by contributor, even if completely gifted.

    b. Foreign LLCs - pursuant to a recent Iowa Supreme Court Decision, qualification for ownership under tenancy by the entireties and charging order protection may be based upon the law of the state where the entity is formed - not where the client is domiciled.

    c. Reminder of importance of following formalities and fiscal management of entities established.

7. SECURE IRA updating:

    a. Set calendar for the year after turning age 72.

    b. Advise clients that spousal rollover planning still works fine.

    c. Advise clients that spousal Conduit Trust planning works the same.

    d. Advise clients that spousal Accumulation Trusts must be paid out within 10 years!

    e. Consider whether the family will be better served by alternative disposition of IRA.

    f. Explain to clients the benefits of a TEA POT Trust.

g. Consider whether the family has a special needs situation which might warrant a TEA CUP Trust or some other type of trust to best hold retirement plan benefits.

8. If the client is over age 72, then the At-Least-As-Rapidly Rule can apply in lieu of the 10-Year Rule upon the client's death, even when the Designated Beneficiary of the retirement plan is an Accumulation Trust for spouse or non-spouse.

9. Consider a Postnuptial/Spousal Accumulation Agreement that would require the owner of a rollover IRA to safeguard the assets for the intended subsequent beneficiaries.

10. Confirm that client knows that life expectancy payouts can only apply for the following:

    a. A spouse, whether the retirement plan is left directly to the spouse, or to a Conduit Trust for the spouse. However, an Accumulation Trust for the spouse will result in a 10-Year-Rule (unless the Accumulation Trust qualifies under the Minor Child Accumulation Trust Exception or an Age 31 Outright Distribution Accumulation Trust).

    b. A disabled or chronically ill beneficiary who qualifies as of the date of death of the Plan Participant, and who is the sole beneficiary individually, or is the sole lifetime beneficiary of a trust that may accumulate distributions - this is the only time when an Accumulation Trust will allow lifetime payouts, unless the At-Least-As-Rapidly Rule applies, because the Plan Participant is over 72 when he or she dies.

    c. An individual, or a Conduit Trust for an individual, who is no more than 10 years younger than the deceased Plan Participant, can receive a life expectancy payout.

    d. The minor child of the deceased Plan Participant can receive a life expectancy payout until reaching age 21, and then the 10-Year Rule will apply from the date of reaching age 21.

11. Consider whether the family would be served by a spousal accumulation agreement.

12. Is the family in a second marriage situation whereby the underlying trust assets would need to be preserved for second level beneficiaries?

13. Remind client that we are in a low interest rate environment which makes wealth transfer vehicles such as GRATs, CLATs, Installment Sales to Grantor Trusts, and QPRTs more attractive.

14. Consider charitable planning and leaving retirement plan assets to charities, whether directly or through Charitable Remainder Unitrust or NIMCRUT.

15. Don't forget creditor protection planning!

CHAPTER 8 – PROPOSED REGULATIONS ON SECURE ACT

The SECURE Act, together with the predecessor Treasury Regulations and IRS Rulings in place (which, as of the enactment of the SECURE Act, did not take into account the changes made by the Act), left us with a web of inconsistent rules that are riddled with gaps requiring many intelligent guesses as to how to design and implement trusts that are funded with IRA/Plan.

On February 24, 2022, the IRS issued very extensive Proposed Regulations, which contain a good many logical and taxpayer-friendly provisions, that seem sure to become permanent in 2022 or early 2023. The Proposed Regulations provide drafters with new strategies that they can begin using in trust agreements and wills that will establish testamentary trusts and provide for flexibility that is permitted under the Proposed Regulations, as described below.

The Preamble provides that in 2022 "taxpayers must apply the existing regulations" in addition to considering "a reasonable, good faith interpretation of the amendments made by sections 114 and 401 of the SECURE Act." By complying with the Proposed Regulations, taxpayers can satisfy this requirement.

The New Required Minimum Distribution System

The Required Minimum Distribution (sometimes abbreviated as "RMD") rules in the Proposed Regulations cover various types of individual beneficiaries and the Plan Participant's estate.

Natalie Choate's recent writings on this topic include the following:

> The new RMD "system" for beneficiaries generally has two parts. First, there is an annual distributions track: What annual distributions are required after the participant's death, if any? Second, there is an "Outer Limit Year" in which 100% of the account becomes the RMD, regardless of what the "annual distributions track" says. To advise a beneficiary you'll need to explain both the annual distributions requirement and the Outer Limit Year requirement. See Prop. Reg. § 1.401(a)(9)-5(e). The post-death payout must be completed in the Outer Limit Year if the account was not previously exhausted by the annual distributions.[118]

To better understand the Required Minimum Distribution for one individual beneficiary of a decedent, Choate identifies three questions that must be answered:

[118] Natalie B. Choate, *The New RMD Rules for Inherited Retirement Accounts*, Ataxplan Publications, 1 (Mar. 17, 2022), https://ataxplan.com/wp-content/uploads/2022/03/How-the-new-RMD-rules-work.pdf.

> 1. Did the decedent die **before or after** his Required Beginning Date ("RBD")? . . . You can NOT figure out any beneficiary's RMDs without knowing whether the decedent died before or on/after her RBD.
>
> 2. What category is the beneficiary? [i.e., is the beneficiary an Eligible Designated Beneficiary, an individual, or an entity?] . . .
>
> 3. [What is] [t]he "beneficiary's life expectancy" (and the decedent's or "ghost" life expectancy)[?][119]

Some of what we cover has to be speculation by necessity, in that the final rules are sure to be somewhat different than what we now have, but the basic structure of what we describe should be sound for present planning.

Eligible Designated Beneficiaries May Qualify for Lifetime Payouts

Before the SECURE Act, almost any person who was the beneficiary of the trust would qualify the trust for either (a) a lifetime payout (as opposed to the 5-Year Rule), or (b) or the "At-Least-As-Rapidly Rule," but the ability to "stretch" IRA distributions out over the life expectancy of a Designated Beneficiary was limited by the SECURE Act to only apply when the applicable beneficiary of the Plan or of the trust that the Plan is payable to is an Eligible Designated Beneficiary.

As described earlier in this Book, the five categories of Eligible Designated Beneficiaries that can utilize the lifetime payments under the SECURE Act are as follows:

(1) The Surviving Spouse;[120]

(2) A minor child[121] of the Plan Participant (defined in the Proposed Regulations as any person under age 21);[122]

(3) A disabled beneficiary;[123]

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[119] *Id.*
[120] Please note that a Surviving Spouse can still roll an IRA or pension made payable solely to him or her into a rollover IRA and under the Proposed Regulation can use the life expectancy of the deceased Plan Participant if he or she was younger than the Surviving Spouse to calculate distributions.
[121] An individual under the age of 21 per the Proposed Regulations.
[122] The use of the stretch rules can only apply until the end of the year in which the child turns 21. The 10-Year Rule will apply in the calendar year following the year in which the child turns 21.
[123] The individual must be disabled on the date of the Plan Participant's death.

(4) A chronically ill beneficiary;[124] or

(5) An individual not more than ten years younger than the deceased Plan Participant.[125]

An Accumulation Trust for the sole benefit of one or more Eligible Designated Beneficiaries can receive payments over the life expectancy of oldest Eligible Designated Beneficiary, but what about other possible beneficiaries who may benefit at a later time? This question is more favorably answered under the Proposed Regulations as discussed below.

The New and "Unimproved" 10-Year Rule

The most unpleasant surprise from the Proposed Regulations concerns the Required Minimum Distributions following the death of a Plan Participant who dies after reaching his or her Required Beginning Date (generally April 1 of the calendar year following the year the Plan Participant reaches the age of 72).

Specifically, the Proposed Regulations state that a beneficiary who inherits an IRA/Plan from such a Plan Participant is required to take distributions beginning on the first calendar year following the year of the Plan Participant's death, and each year thereafter until the 10th year following the calendar year of the Plan Participant's death when all assets in the IRA/Plan must be distributed from the IRA/Plan to such beneficiary.

This is a change from the "10-Year Rule" under the statute as understood by many practitioners and commentators, where the beneficiaries of the deceased Plan Participant's Retirement Plan who are subject to the 10-Year Rule would not be required to take any distributions following the death of the Plan Participant until December 31 of the 10th year following the calendar year of the Plan Participant's death (regardless of the Plan Participant's age at death).

Many practitioners and commentators find this IRS interpretation to be shocking, since a parallel "5-Year Rule" has been in effect under the Internal Revenue Code and Treasury Regulations regarding Retirement Plans for decades, and such 5-Year Rule has never been interpreted or construed to require distributions to be made from the Retirement Plan before December 31 of the 5th year following the Plan Participant's death.

Nevertheless, authorities in this area have expressed concern that taxpayers and trusts may be severely penalized for failure to take distributions under rules that are very difficult to understand. As such, trustees may wish to err on the side of caution and take Required Minimum Distributions during the initial ten years if this will not have a significant tax impact.

The Proposed Regulations interpret the 10-Year Rule differently if the Plan Participant died prior to his or her Required Beginning Date, in which case the 10-Year Rule operates in a similar manner to the historical 5-Year Rule. In other words, no distributions are required to be made from the IRA/Plan until December 31 of the 10th year following the calendar year of the Plan Participant's death, if he or she died before the Required Beginning Date.

[124] The individual must be chronically ill on the date of the Plan Participant's death.
[125] Most commonly a sibling.

Designated and Disregarded Beneficiaries

The Proposed Regulations identify two tiers of Designated Beneficiaries.[126] Tier I includes any beneficiaries of the trust whose benefits “are neither contingent upon nor delayed until the death of another trust beneficiary” who did not predecease the Plan Participant. Tier II includes “any beneficiaries of the trust who could receive amounts in the trust . . . that were not distributed to the [Tier I] beneficiaries, [but only if they cannot benefit until after the death of the Tier I beneficiary or beneficiaries].” If the beneficiary of the See-Through Trust is another trust, the beneficiaries of the second trust are treated as being beneficiaries of the first trust and thus they are considered Designated Beneficiaries.

There are multiple situations under the Proposed Regulations in which a beneficiary can be “disregarded” for purposes of determining which payout method applies:

1. If one of the following events occur prior to September 30th of the calendar year following the year of the Plan Participant’s death:

   A. A beneficiary predeceases the Plan Participant.

   B. A beneficiary is treated as having predeceased the Plan Participant by reason of a simultaneous death provision under applicable state law or via a qualified disclaimer.

   C. A beneficiary receives the entire benefit that the beneficiary is entitled to.

   D. If a power of appointment is exercised in favor of one or more beneficiaries, then the other permissible appointees are disregarded.

There are also situations under the Proposed Regulations where trust beneficiaries will be disregarded even if their interest is not eliminated prior to the September 30th Designation Date:

1. <u>An Accumulation Trust Beneficiary Who Can Only Benefit After the Death of Tier I and Tier II Beneficiaries.</u> For Accumulation Trusts only, when entitlement of such beneficiary is conditioned upon the death of any and all Tier I Beneficiaries and at least one Tier II Beneficiary, this type of beneficiary sometimes is referred to as a “Tier III Beneficiary.”

The Preamble to the Proposed Regulations provides the following example to illustrate this rule:

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[126] § 401(a)(9) did not categorize designated beneficiaries, however §1.401(a)(9)-(4)(f)(3)(I) provides that “[a]ny beneficiary who could receive amounts in the trust representing the employee’s interest in the plan that are neither contingent upon, nor delayed until, the death of another trust beneficiary who did not predecease (and is not treated as having predeceased) the employee; and any beneficiary of an accumulation trust that could receive amounts in the trust representing the employee’s interest in the plan that were not distributed to beneficiaries.”

> [A]ssume that an IRA names a see-through accumulation trust that requires the trustee to pay specified amounts from the trust to the employee's surviving spouse. Upon the spouse's death, the see-through trust is to terminate and the amounts remaining in the trust are to be paid to the employee's brother (who is not more than 10 years younger than the employee, and thus is an Eligible Designated Beneficiary). Further if the employee's brother survives the employee but predeceases the surviving spouse, then the amounts remaining in the trust after the death of the surviving spouse are to be paid to a charity.
>
> In that case, the charity is disregarded as a beneficiary of the employee because the charity could receive only amounts in the trust that are contingent upon the death of the employee's brother, whose only interest was a residual interest (that is, an interest in the amounts remaining in the trust after the death of the surviving spouse).
>
> In contrast, the charity would be treated as a beneficiary of the employee if the brother could receive amounts in the trust not subject to any contingencies or contingent upon an event other than the death of the surviving spouse (such as the surviving spouse's remarriage).

2. <u>A Beneficiary Who Can Only Inherit by Surviving a Minor Under a Trust That Pays Out Entirely On or Before the Minor's 31st Birthday (The "Age 31 Outright Distribution Accumulation Trust").</u> A beneficiary of a See-Through Trust may also be disregarded when entitlement is conditioned upon the death of a minor (not necessarily a minor child of the Plan Participant) who has not reached the age of majority (21) if the terms of the trust requires full distribution to such minor by the <u>later</u> of (1) the 10th calendar year following the calendar year of the Plan Participant's death, or (2) the end of the 10th calendar year following the calendar year in which that minor attains age 21.[127]

The following example from the Preamble illustrates this rule:

> Assume an employee names an [Accumulation] trust as the sole beneficiary, the trust permits specified amounts to be paid to the employee's niece until the niece reaches age 31 (age of majority plus 10 years). The trust is scheduled to terminate with a full distribution of all trust assets to the niece when the niece reaches age 31, but if the niece dies before this scheduled termination, then the amounts remaining in the trust will be paid to the employee's sibling. In that case, the only beneficiary designated under the plan for purposes of section 401(a)(9) and these regulations is the employee's niece because the employee's sibling is disregarded under the exception described in the preceding paragraph.
>
> However, if the see-through trust terms do not require a full distribution of amounts in the trust representing the employee's interest in the plan until the niece reaches

[127] § 1.401(a)(9)-4(f)(3)(ii).

age 35, then this exception does not apply, and both the employee's niece and sibling are treated as beneficiaries designated under the plan for purposes of section 401(a)(9) and these regulations.

3. Remainder Beneficiaries of Conduit Trusts Continue to Be Disregarded. Remainder beneficiaries of Conduit Trusts continue to be disregarded. In other words, only beneficiaries that could receive amounts in trust that are neither contingent upon, nor delayed until, the death of another trust beneficiary (Tier I Beneficiaries) must be taken into account.

The following example derived from the Proposed Regulations illustrate this rule:[128]

Cathy dies at the age of 30 leaving her retirement plan payable to a trust for the benefit of her 35 year old sibling Doug. If and when Doug dies, the trust will pass to Edward, who is 50.

Doug is an Eligible Designated Beneficiary because he is not less than ten years younger than Cathy. Since the trust is a Conduit Trust, Edward's interest can be disregarded and distributions can be paid out over Doug's life expectancy as an Eligible Designated Beneficiary; however if the Trust was an Accumulation Trust, Edward would be considered a designated beneficiary and, since all trust beneficiaries are not Eligible Designated Beneficiaries, the 10-Year Rule would apply.

If the Accumulation Trust instead provided that it was for the benefit of Doug, and that after the death of Doug the trust would be held for the sole benefit of Cathy's 36 year old half-sibling Frank, and then would only benefit Edward if both Doug and Frank were deceased, then Edward would be disregarded and the

[128] Adaptation from Example 1 in the Proposed Regulations under § 1.401(a)(9)-4(f)(6). **(A) Facts.** Employer L maintains a defined contribution plan, Plan W. Unmarried Employee C died in 2022 at age 30. Prior to C's death, C named a testamentary trust (Trust T) that satisfies the requirements of paragraph (f)(2) of this section, as the beneficiary of C's interest in Plan W. The terms of Trust T require that all distributions received from Plan W, upon receipt by the trustee, be paid directly to D, C's sibling, who is 5 years older than C. The terms of Trust T also provide that, if D dies before C's entire account balance has been distributed to D, E, will be the beneficiary of C's remaining account balance. **(B) Analysis.** Pursuant to paragraph (f)(1)(ii)(A) of this section, Trust T is a conduit trust. Because Trust T is a conduit trust (meaning the residual beneficiary rule in paragraph (f)(3)(i)(B) of this section does not apply) and because E is only entitled to any portion of C's account if D dies before the entire account has been distributed, E is disregarded in determining C's designated beneficiary. Because D is an eligible designated beneficiary, D may use the life expectancy rule of § 1.401(a)(9)-3(c)(4). Accordingly, even if D dies before C's entire interest in Plan W is distributed to trust T, D's life expectancy continues to be used to determine the applicable denominator.

lifetime payment rules could apply since all beneficiaries are Eligible Designated Beneficiaries.

Just a "Minor" Exception for Accumulation Trusts

As a general rule, if an Accumulation Trust has a Designated Beneficiary who is not an Eligible Designated Beneficiary, then the Plan Participant is treated as NOT having an Eligible Designated Beneficiary, and thus the IRA must be distributed no later than the end of the 10th year following the calendar year of the Plan Participant's death.

The Proposed Regulations introduce a new exception to this rule if there is a Designated Beneficiary who is the child under age of majority of the Plan Participant (the Minor Child Accumulation Trust Exception). In this case, the Plan Participant is treated as having an Eligible Designated Beneficiary allowing life expectancy payments to be made until ten years after the year in which the child reaches age 21.

The following examples from the Preamble illustrate this rule:

> A Plan Participant names a see-through trust as the sole beneficiary of the employee's interest in the plan, and the trust beneficiaries are the employee's surviving spouse and the employee's adult child who is neither disabled nor chronically ill, then the employee is treated as not having an Eligible Designated Beneficiary. As a result, the employee's entire interest must be distributed no later than 10 years after the employee's death.
>
> However, if there is another Designated Beneficiary who is the employee's child and who, as of the date of the employee's death, has not yet reached age 21, then, under the exception described in the preceding paragraph, the employee is treated as having an Eligible Designated Beneficiary. In the situation described in the preceding sentence, if the trust is receiving annual distributions using the life expectancy rule, then a full distribution from the plan would not be required until ten years after the year in which the minor child reaches age 21.

Changes for Disabled and Chronically Ill Beneficiaries

To summarize briefly, a beneficiary is considered to be disabled or chronically ill if they satisfy the applicable definition as of the Plan Participant's date of death and meet certain documentation requirements no later than October 31 of the calendar year following the calendar year of the Plan Participant's death.

The Proposed Regulations do not provide new guidance with respect to defining "chronically ill," and also do not change the definition of "disabled" for beneficiaries who are 18 years of age or older. The Proposed Regulations do provide a new definition of "disabled" for beneficiaries under the age of 18, and also confirm that if a beneficiary is considered to be disabled as of the date of death by the Commissioner of Social Security under the definition of 42 U.S.C. 1382c (a)(3), then such beneficiary will be considered disabled for purposes of the Required Minimum Distribution rules regardless of age.

A disabled beneficiary is defined as follows:

Age 18 or older - An individual who, as of the date of the employee's death, is age 18 or older is disabled if, as of that date, the individual **is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment** that can be expected to result in death or to be of long continued and indefinite duration.

Younger than Age 18 - An individual who, as of the date of the employee's death, is **not** age 18 or older is disabled if, as of that date, that individual **has a medically determinable physical or mental impairment that results in marked and severe functional limitations** and that can be expected to result in death or to be of long continued and indefinite duration.

Further, the Proposed Regulations delineate a category of See-Through Trusts that have at least one disabled or chronically ill beneficiary and they are called Applicable Multi-Beneficiary Trusts.

An "Applicable Multi-Beneficiary Trust" is a See-Through Trust with more than one beneficiary that will benefit one or more disabled or chronically ill individuals, and with respect to which [both of the following apply]:

(1) all of the trust beneficiaries are Designated Beneficiaries; and

(2) at least one of the trust beneficiaries is an Eligible Designated Beneficiary who is disabled or chronically ill.[129]

There are two types of Applicable Multi-Beneficiary Trusts, Type I and Type II.

A Type I Multi-Beneficiary Trust is a trust which provides that the amounts in trust are to be divided immediately upon the death of the Plan Participant into separate trusts for each beneficiary.[130]

A Type II Multi-Beneficiary Trust is a trust that both:

(1) Identifies one or more individuals who are disabled or chronically ill and entitled to benefits during his/her lifetime, and

[129] The Proposed Regulations clarify §401(a)(9)(H)(v) and provide that "[a]n applicable multi-beneficiary trust is a see-through trust with more than one beneficiary and with respect to which— (i) All of the trust beneficiaries are designated beneficiaries; and (ii) At least one of the trust beneficiaries is an eligible designated beneficiary who is disabled . . . or chronically ill." §1.401(a)(9)-4(g).
[130] § 1.401(a)(9)-4(g)(2).

(2) Provides that no individual who is not disabled, chronically ill, or entitled to benefits during their lifetime "has any right to . . . interest in the plan until the death of all of the Eligible Designated Beneficiaries who are disabled, chronically ill, and entitled to receive benefits during their lifetime."[131]

One of the separate trusts under a Type I Multi-Beneficiary Trust to which the amounts are divided can be a Type II Multi-Beneficiary Trust. The beneficiaries of the receiving Type II Multi-Beneficiary Trust who are not disabled or chronically ill will be disregarded for purposes of these regulations, thus allowing for payments to be made from the IRA over the life expectancy of the disabled or chronically ill beneficiary. However, if the terms of the trust fail to comply with the requirements of a Type II Multi-Beneficiary Trust then all of the beneficiaries are treated as beneficiaries.[132]

Use of Powers of Appointment Under the Proposed Regulations – A New Safe Harbor

Generally, the Proposed Regulations adopt a very taxpayer-friendly view of Powers of Appointment. Essentially, an individual is permitted to hold the power to direct trust assets to one or more individuals, creditors, or charities without causing the trust to fail the identifiability requirement of See-Through Trusts, and without such permissible appointees being considered to be beneficiaries of the trust for purposes of determining Required Minimum Distributions from the IRA/Plans, if properly drafted before death and handled after death.

The Basics

A Power of Appointment is a right given to an individual in a non-fiduciary capacity (the "powerholder") to direct how trust assets will pass. There are two ways to characterize a Power of Appointment: (1) when the power can be exercised, and (2) how the power can be exercised.

I. When The Power Can Be Exercised

A Power of Appointment can be exercised (a) during the lifetime or upon the death of the powerholder, or (b) only after the death of the powerholder. These are called Lifetime Powers of Appointment and Testamentary Powers of Appointment, respectively.

A "Lifetime Power of Appointment" will normally provide the individual powerholder with the ability to direct where Trust assets will be paid at any time during their lifetime. A "Testamentary Power of Appointment" is exercisable only upon the death of the powerholder.

[131] §1.401(a)(9)-4(g)(3).

[132] The special rule concerning Type II Multi-Beneficiary Trusts was originally in §401(a)(9)(H)(iii) and §1.401(a)(9)-4(g)(3)(ii) amends such provision to read as follows: "[i]f an employee's beneficiary is a type II applicable multi-beneficiary trust . . . then the beneficiaries of the trust [other than the disabled or chronically ill beneficiary] are treated as eligible designated beneficiaries without regard to whether any of the other trust beneficiaries are not eligible designated beneficiaries."

II. How the Power Can Be Exercised.

A Power of Appointment can also vary in the extent to which the power can be exercised. A powerholder either has unrestricted power to direct the passage of trust assets or is limited to a certain group or class of beneficiaries to whom the powerholder can direct assets to. The two types of Power of Appointments under this category are "General Powers of Appointment" and "Limited Powers of Appointment."[133] A General Power of Appointment is a Power of Appointment that includes the power to appoint assets to one or more of (a) the powerholder, (b) the powerholder's estate, (c) the powerholder's creditors, or (d) the creditors of the powerholder's estate. A Limited Power of Appointment is a power of appointment that is not a General Power of Appointment (i.e., the powerholder does not have any power to appoint assets to one of the four aforementioned categories of appointees).

Example - General Power of Appointment

Jack creates a trust and directs the trustee to pay the income to his child, Sally, for Sally's life. Upon Sally's death, the property is to pass to Sally's children. Sally is given the power to appoint the property to her own estate upon her death. If she exercises the power, the property will pass pursuant to the terms of Sally's Last Will and Testament (rather than pursuant to the terms of the trust). Sally possesses a testamentary General Power of Appointment, even though she does not personally benefit from the exercise of the Power of Appointment.

Example - Limited Power of Appointment

Jack creates a trust to pay the income to Sally for life and then to pay the remainder to Sally's children. Jack also gives Sally the power to make distributions for the health, education, maintenance and support of Sally's husband, Steve, during her lifetime. Sally holds a lifetime Limited Power Of Appointment because her power to distribute is limited by an ascertainable standard relating to the health, education, maintenance or support of her husband. Sally may not exercise the power in favor of herself, her estate, her creditors, or creditors of her estate.

<u>See-Through Trusts</u>

A popular tax planning tool for IRA/Plan owners is the use of See-Through Trusts. A See-Through Trust is a trust that acts as the beneficiary of a Plan Participant's retirement account. The Plan Participant makes the beneficiaries of the trust the individuals for whom the Plan Participant wishes to pass such assets. See-Through Trusts get their name because you can "see through" the

[133] Typically, a Power of Appointment provided in a Trust document will permit the Surviving Spouse (or a child) to redirect how the trust assets will pass on his or her death, and will be limited to being exercisable only to or for the benefit of the descendants of the powerholder or of the settlor of the trust. To avoid the powerholder being treated as the owner of assets subject to the power for federal estate tax (and creditor purposes in some states), the power should not be exercisable in favor of the powerholder, the powerholder's estate, the powerholder's creditors, or the creditors of the powerholder's estate. A power limited to being exercisable solely in favor of descendants of the powerholder will not be considered exercisable in favor of the powerholder, the powerholder's estate, the powerholder's creditors, or the creditors of the powerholder's estate.

trust to the underlying beneficiaries. However, to qualify as a See-Through Trust, the underlying beneficiaries must be identifiable.

With reference to the identifiability requirement for See-Through Trusts, the Proposed Regulations provide that "if it is possible to identify each person eligible to receive a portion of . . . the plan through the trust" the requirement is met. Previously, the presence of a Power of Appointment (whether it was exercisable in favor of creditors, charities, or other "non-persons") was thought by many to possibly cause such requirement to not be met because the failure of the powerholder to exercise or restrict such power resulted in the inability to determine who the beneficiaries are, particularly when such Power was not limited to a specific class of beneficiaries. As such, all permissible appointees under a Power of Appointment were to be taken into account for the purposes of determining the Designated Beneficiary of the IRA/Plan.

In addition, if the Power was exercisable in favor of creditors, charities, or other "non-persons," they would be viewed as beneficiaries of the trust, and thus cause the IRA/Plan to be considered to have a non-individual beneficiary and subject to less favorable payout rules. Many planners' documents contained specific language to provide that the Power of Appointment could only be exercised in favor of individuals that were younger than the powerholder to prevent the permissible appointment of trust assets in favor of an older beneficiary that might impact the ability to stretch distributions out over the lifetime of the oldest beneficiary of the trust.

The Proposed Regulations, however, provide a safe harbor for See-Through Trusts by identifying the beneficiaries when a Power of Appointment exists.

Under the Proposed Regulations, the mere existence of a Power of Appointment will not cause the trust to fail the identifiability requirement, or cause all potential appointees of the Power of Appointment to be taken into account for the purposes of determining the Designated Beneficiary. Rather, Powers of Appointment would be treated in three different ways depending upon the applicable circumstances. Each of the circumstances is relative to whether the power was exercised or restricted as of September 30th in the calendar year following the calendar year in which the Plan Participant died (i.e., the "Designation Date").

1. <u>Power Exercised or Restricted by Designation Date</u>.

If the powerholder exercises or restricts the Power prior to the Designation Date, the persons who benefit as a result of such exercise are considered to be beneficiaries of the trust.

Alternatively, the power may be restricted to only be exercisable in favor of only two or more identifiable beneficiaries before the Designation Date, in which case the permissible appointees under the restricted power are considered to be the beneficiaries of the trust.

Specifically the Proposed Regulation reads as follows:

> Power of Appointment - (A) Exercise or release of Power of Appointment by September 30.

> A trust does not fail to satisfy the identifiability requirements of this paragraph (f)(5) merely because an individual (powerholder) has the power to appoint a portion of the employee's interest to one or more beneficiaries that are not identifiable within the meaning of paragraph (f)(5)(i) of this section. If the Power of Appointment is exercised in favor of one or more identifiable beneficiaries by September 30 of the calendar year following the calendar year of the employee's death, then those identifiable beneficiaries are treated as beneficiaries designated under the plan. The preceding sentence also applies if, by that September 30, in lieu of exercising the Power of Appointment, the powerholder restricts it so that the power can be exercised at a later time in favor of only two or more identifiable beneficiaries (in which case, those identified beneficiaries are treated as beneficiaries designated under the plan).

2. <u>Failure to Exercise or Restrict Power by Designation Date</u>.

If the powerholder does not exercise the power by the Designation Date in favor of one or more beneficiaries that are identifiable, or the power is not so restricted, then each Taker in Default (each person who would be entitled to the portion subject to the power if that power is not exercised) is treated as a beneficiary of the IRA/Plan.

Specifically the Proposed Regulations read as follows:[134]

> However, if, by that September 30 [i.e., the Designation Date], the Power of Appointment is not exercised (or restricted) in favor of one or more beneficiaries that are identifiable within the meaning of paragraph (f)(5)(i) of this section, then each taker in default (that is, any person that is entitled to the portion that represents the employee's interest in the plan subject to the Power of Appointment in the absence of the powerholder exercising the power) is treated as a beneficiary designated under the plan.

3. <u>Power Exercised or Restricted after Designation Date</u>.

If the powerholder fails to exercise or restrict the power prior to the Designation Date, but instead does so thereafter, then those who it is exercised in favor of will be treated as beneficiaries of the trust, and the trust must be "re-tested" to determine the new payout schedule for Required Minimum Distributions.

Specifically the Proposed Regulations read as follows:[135]

> (B) Exercise of Power of Appointment after September 30 of the calendar year following the calendar year of the employee's death.

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[134] Prop. Reg. § 1.401(a)(9)-4(f)(5)(ii)(A), 87 Fed. Reg. 10504 (Feb. 24, 2022).
[135] Prop. Reg. § 1.401(a)(9)-4(f)(5)(ii)(B), 87 Fed. Reg. 10504 (Feb. 24, 2022).

If an individual has a Power of Appointment to appoint a portion of the employee's interest to one or more beneficiaries and the individual exercises the Power of Appointment after September 30 of the calendar year following the calendar year of the employee's death, then the rules of paragraph (f)(5)(iv) of this section apply with respect to any trust beneficiary that is added pursuant to the exercise of the Power of Appointment.

(f)(5)(iv) Addition of beneficiary after September 30.

If, after September 30 of the calendar year following the calendar year of the employee's death, a trust beneficiary described in paragraph (f)(3) of this section is added as a trust beneficiary (whether through the exercise of a Power of Appointment, the modification of trust terms, or otherwise), then—

(A) The addition of the beneficiary will not cause the trust to fail to satisfy the identifiability requirements of this paragraph (f)(5);

(B) Beginning in the calendar year after the calendar year in which the new trust beneficiary was added, the rules of § 1.401(a)(9)-5(f)(1) will apply taking into account the new beneficiary and all of the beneficiaries of the trust that were treated as beneficiaries of the employee before the addition of the new beneficiary; and

(C) Subject to paragraph (f)(5)(v) of this section, the rules of paragraphs (b) and (e)(2) of this section and § 1.401(a)(9)-5(f)(2) will apply taking into account the new beneficiary and all of the beneficiaries of the trust that were treated as beneficiaries of the employee before the addition of the new beneficiary.

The following examples provided by the authors, which are based on examples in the Proposed Regulations, demonstrate the aforementioned scenarios.

Our Example One - Restriction of Power of Appointment Prior to Designation Date

Dad died in 2022 at the age of 60. Dad named a See-Through Trust as a beneficiary of his IRA. Under the terms of the trust, all trust income is payable to Dad's Surviving Spouse, Mom, and Mom has a Power of Appointment to redirect the trust assets upon her death. The Power of Appointment provides that, if Mom does not exercise the power, then upon Mom's death, Dad's descendants, per stirpes, are entitled to the remainder interest. As of the date of Dad's death, Dad has two adult children, Child 1 and Child 2.

Before the Designation Date, Mom irrevocably restricts Mom's Power of Appointment so that Mom may only exercise the power to appoint in favor of Mom's siblings (who all are less than 10 years younger than Dad and thus, are Eligible Designated Beneficiaries).

Because Mom timely restricted the Power of Appointment so that Mom may exercise the power only in favor of Mom's siblings, the only Designated Beneficiaries are Mom and Mom's siblings, even though Child 1 and Child 2 are the Takers in Default. Because all of the Designated Beneficiaries are Eligible Designated Beneficiaries, payments may be made over Mom's life expectancy.

Our Example Two - Restriction of Power of Appointment Prior to Designation Date

A See-Through Trust established on the death of the Plan Participant benefits a Surviving Spouse, and children of the Plan Participant who are over the age 21 after the death of the Surviving Spouse. The Surviving Spouse has a Limited Power of Appointment. This structure will cause the Trust to be subject to the 10-Year Rule. In order to qualify for a lifetime payout instead of the 10-Year Rule apply, only Eligible Designated Beneficiaries must be considered the beneficiaries of the Trust. Since the adult children are non-Eligible Designated Beneficiaries, the lifetime payout is not allowed and the 10-Year Rule applies. To remedy this issue, the Surviving Spouse’s Power of Appointment can be restricted before the September 30th Designation Date to provide that the Surviving Spouse may only appoint assets to the Plan Participant's surviving brother, who is less than ten years younger than the Plan Participant, and is therefore an Eligible Designated Beneficiary. As a result of the above, the Life Expectancy Payout Method can be used instead of the 10-Year Rule.

The practical implications of this must also be considered. While this would allow for a more advantageous payout for tax purposes, the Surviving Spouse would lose the ability to redirect or reallocate how the Trust assets pass upon her death between the children. For example, if one child fell out of favor, or another child needed a larger percentage of the assets, and the Power of Appointment was modified or restricted as provided above, then the Surviving Spouse could not exercise the Power to accomplish this reallocation. There may however be non-IRA assets over which the Surviving Spouse could have a Power of Appointment in favor of the children and could accomplish the reallocation via exercise of the power over non-IRA assets.

Our Example Three - Failure to Exercise or Restrict Power of Appointment Prior to Designation Date

Assuming the same facts as Example One above, if Mom did not timely restrict the Power of Appointment, then Mom, Child 1 and Child 2 would all be considered Designated Beneficiaries and the 10-Year Rule would apply since not all Designated Beneficiaries are Eligible Designated Beneficiaries.

As illustrated by the above examples, the restriction of a Power of Appointment can be useful to ensure that the Uniform Life Expectancy Method applies for Eligible Designated Beneficiaries by restricting its exercise to only be in favor of Eligible Designated Beneficiaries, even if the takers in lieu of exercise of such power are non-Eligible Designated Beneficiaries.

Drafting and Interpretation Issues?

As mentioned above, the Proposed Regulations provide that when a powerholder restricts the Power of Appointment so that the Power can be exercised at a later time in favor of only two or more identifiable beneficiaries, then those identifiable beneficiaries are treated as Designated Beneficiaries under the Plan, and the takers in default can be ignored for stretch trust rule purposes.

This particular section of the Proposed Regulations may leave practitioners with questions regarding the status of potential takers in default.

Based on the plain reading of the language, the Proposed Regulations seem to provide that the mere act of restricting a Power of Appointment prior to the Determination Date to be exercisable in favor of two or more "identifiable beneficiaries" will cause those identifiable beneficiaries to be considered to be beneficiaries of the trust (even though they are not actually beneficiaries for state law purposes, and may therefore not be entitled to be told about the existence of the trust, to receive accountings with respect to the trust, or to otherwise have the rights that are accorded to beneficiaries under state law).

However, a question arises as to whether the "takers in default" of the Power of Appointment will be counted as beneficiaries under these rules if they can only benefit after the death of the powerholder if the Power of Appointment is not exercised. Generally takers in default, as Tier II Beneficiaries, would be included in the calculation - are they simply disregarded upon restriction of the Power of Appointment?

An example provided in the Proposed Regulations is in accordance with that result. In the example, a 60-year old Plan Participant dies leaving an IRA or pension account to a properly drafted Accumulation Trust for the lifetime benefit of his Surviving Spouse, with the remainder of the trust to pass to his two children who are not disabled or chronically ill and are both older than age 21. Before September 30 of the calendar year following the year in which the participant died, the Surviving Spouse irrevocably restricts her Power of Appointment to be exercisable only in favor of siblings who were less than 10 years younger than the Plan Participant "and thus, are eligible Designated Beneficiaries." The example concludes that the children are the "takers in default" under the Power of Appointment and are not counted as beneficiaries.

The example, in its entirety, reads as follows:

> (A) Facts related to plan and beneficiary. Employer N maintains a defined contribution plan, Plan Y. Employee F, an employee of N, died in 2022 at the age of 60. F named a testamentary trust (Trust Q), which was established under F's will, as the beneficiary of all amounts payable from F's account in Plan X after F's death. Trust Q satisfies the see-through trust requirements of paragraph (f)(2) of this section.
>
> (B) Facts related to trust. Under the terms of Trust Q, all trust income is payable to F's surviving spouse, G, and G has a Power of Appointment to name the beneficiaries of the residual in Trust Q. The Power of Appointment provides that,

> if G does not exercise the power, then upon G's death, F's descendants are entitled to the remainder interest in Trust Q, per stirpes. As of the date of F's death, F has two children, K and L, who are not disabled or chronically ill and who are both older than age 21. Before September 30 of the calendar year following the calendar year in which F died, G irrevocably restricts G's Power of Appointment so that G may exercise the power to appoint the remainder beneficiaries of Trust Q only in favor of G's siblings (who all are less than 10 years younger than F and thus, are eligible designated beneficiaries).
>
> (C) Analysis. Pursuant to paragraph (f)(5)(ii)(A) of this section, because G timely restricted the Power of Appointment so that G may exercise the power to appoint the residual interest in Trust Q only in favor of G's siblings, the designated beneficiaries are G and G's siblings. Because all of the designated beneficiaries are eligible designated beneficiaries, annual life expectancy payments are permitted under section 401(a)(9)(B)(iii). Note, however, that because § 1.401(a)(9)-5(e) applies, a distribution of the remaining interest is required by no later than 10 years after the calendar year in which the oldest of G and G's siblings dies.
>
> Based on the above example from the IRS, F's descendants, K and L would be the takers in default. Here, G timely restricted the Power of Appointment in favor of only G's siblings and the restriction resulted in only G and G's siblings being counted as designated beneficiaries under the Plan.

The above example does not explicitly mention what happens to the takers in default, but seems to provide that the restriction eliminates them from being included as beneficiaries of the trust.

Alternatively, the Proposed Regulations could be interpreted to provide that those beneficiaries who are potential appointees under a restricted Power of Appointment are considered as "countable" for purposes of determining the post-death payout schedule as well as the takers in default, unless or until the Power of Appointment is actually exercised. Under this interpretation, regardless of a restriction put on a Power of Appointment in favor of two or more identifiable beneficiaries, unless the Power is exercised in their favor, the takers in default will be used in determining the post-death payout schedule. However, this interpretation conflicts with the language of the example provided in the Proposed Regulations.

It is also not clear what happens if the Power of Appointment is restricted only in favor of one identifiable beneficiary prior to the Designation Date. The Proposed Regulations state that if the powerholder "restricts [the power] so that the power can be exercised at a later time in favor **<u>of only two or more</u>** identifiable beneficiaries" [emphasis added], then the permissible appointees under the Power are considered the beneficiaries and not the takers in default. But what if the Power is restricted to only permit the appointment to one identified individual, such as the spouse's brother who is not more than ten years younger than the Plan Participant? Are the takers in default also considered to be beneficiaries because the power is not exercisable in favor of *two or more* beneficiaries? Is the brother the only beneficiary of the trust for purposes of the required minimum distribution rules, and this is just a drafting error? The Preamble and the actual text of the Proposed Regulations appear to be in conflict on this.

The Preamble indicates that "[s]pecifically, these proposed regulations provide that if, by September 30 of the calendar year following the calendar year of the employee's death, the power is exercised in favor of one or more beneficiaries that are identifiable or is ***restricted so*** that any appointment made at a later time may only be made ***in favor of one or more*** identifiable beneficiaries, then all of those identifiable beneficiaries are taken into account as beneficiaries of the employee." [emphasis added]

It appears that the Preamble expected the Proposed Regulations language to require the power to be restricted so that a Power of Appointment could only be exercised in favor of "one or more" individuals while the actual text of the Proposed Regulations provides that the power must be restricted in "favor of only two or more" individuals. The authors believe that these conflicting provisions are mistakes in the drafting of the provisions rather than intentional conflicts.

Hopefully this will be cleared up in the Final Regulations after comments have been made.

Addition of Beneficiary After Designation Date

The Proposed Regulations also provide a new rule that applies when a beneficiary is added who was not initially taken into account in determining the Designated Beneficiary of the IRA/Plan.

Under this rule, if a beneficiary is added after the Designation Date, then the eligibility of the See-Through trust is re-evaluated alongside the Required Minimum Distribution method that is utilized. The rules regarding multiple Designated Beneficiaries[136] must be applied when evaluating the effect of the newly added beneficiary along with all of the beneficiaries that were taken into account before the addition of the new beneficiary.[137]

[136] The Proposed Regulations provide that if an IRA/Plan has more than one Designated Beneficiary and one of them is not an Eligible Designated Beneficiary, then for purposes of section 401(a)(9), the IRA/Plan generally is treated as not having an Eligible Designated Beneficiary. In addition, the Proposed Regulations provide that if the Surviving Spouse is waiting to begin distributions until the year in which the IRA/Plan Participant would have attained age 72 and the Surviving Spouse died before the beginning of that year, then the determination of whether the Surviving Spouse's Designated Beneficiary is an Eligible Designated Beneficiary is made by substituting the Surviving Spouse for the employee (including for purposes of establishing the date as of which that determination is made). For example, a child of the Surviving Spouse is an Eligible Designated Beneficiary if the child has not yet reached the age of majority as of the date of the Surviving Spouse's death.

[137] Instead of determining the applicable denominator using the beneficiary with the shortest life expectancy, the Proposed Regulations provide that the applicable denominator is determined using the life expectancy of the oldest Designated Beneficiary. The Proposed Regulations also provide that whether a full distribution is required is generally determined using the oldest of the designated beneficiaries. By example, if an employee has multiple Eligible Designated Beneficiaries who are born in the same calendar year, then full distribution of the employee's remaining interest generally must be completed by the 10th calendar year following the death of the oldest Designated Beneficiary.

Alternatively, if the addition of the beneficiary would cause a full distribution of the employee's interest in the plan to be required pursuant to Section 401(a)(9)(H) during the calendar year in which the beneficiary is added or in an earlier calendar year, then the Proposed Regulations provide that the full distribution is not required until the end of the calendar year following the calendar year in which the beneficiary was added.

Other Power of Appointment Considerations

Powers of Appointment are used for many reasons, including to give trusted family members the ability to redirect how trust assets may pass, and for generation-skipping tax planning situations where a family has large trusts that may be subject to the federal generation-skipping tax. A power given to a beneficiary to direct trust assets to creditors, or creditors of his or her estate, can be used to avoid imposition of federal generation-skipping tax on the death of a beneficiary.[138]

In addition, a Power of Appointment may be used to facilitate a step-up in basis for appreciated assets held in trust.[139] The mere possession of a General Power of Appointment over an appreciated asset at the time of the decedent's death can cause such property to be included in the powerholder's estate irrespective of whether the power was actually exercised. The basis in the property will "step up" to the fair market value of the property at the decedent's death, thus when the property is later sold the possible capital gain on the property will be far less than if the property had the lower basis.[140]

Under certain circumstances, planners may also give independent parties who are not fiduciaries the ability to convert Limited Powers of Appointment to General Powers of Appointment in order to provide for a step-up in basis if estate tax is not a concern.

It is noteworthy that a Power of Appointment can exist and be considered to be exercisable under the Treasury Regulations for income tax and estate tax purposes, notwithstanding that it can only be effective if approved by one or more independent persons ("non-adverse parties") whose power of approval is not subject to a fiduciary duty.[141]

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[138] See Blattmachr, Rivlin & Slade, *Selected Planning and Drafting Aspects of Generation-Skipping Transfer Taxation*, for an in-depth discussion on the use of Powers of Appointment in generation-skipping tax planning situations. https://shenkmanlaw.com/uploads/2021/04/Generation-Jumping-Selected-Planning-and-Drafting-Aspects-of-Generation-Skipping-Transfer-Taxation-2.pdf. Jonathan Blattmachr is said to have invented the Power of Appointment just after inventing the installment sale to the grantor trust. His presentations on Powers of Appointment are unsurpassed.

[139] It is noteworthy that assets held in an IRA/Plan (or assets otherwise containing income in respect of decedent) do not receive the step-up in basis, pursuant to IRC § 1014(c).

[140] See Ed Morrow on PLR 202206008: Judicial Settlement Modification & Formula Testamentary General Powers of Appointment. Leimberg Information Services. March 17, 2022. https://www.leimbergservices.com/openfile.cfm?filename=c:\inetpub\wwwroot\all\lis_notw_2946.html&fn=lis_notw_2946.

[141] See IRC § 2041. See also Blattmachr, Rivlin & Slade, "Selected Planning and Drafting Aspects of Generation-Skipping Transfer Taxation," Financial Planning Thoughts 1996. "A person is treated as holding a general (taxable) Power of Appointment under IRC § 2041 even if it is exercisable with the consent of a non-adverse party (that is,

For example, giving an elderly individual the power to direct assets to creditors of her estate could be somewhat dangerous as there is a risk that someone might take advantage of her and have her sign a promissory note to them and subsequently appoint assets in the Trust upon her death to pay the note.

If long-time friends or neighbors have the power to approve or veto the exercise of the power on a non-fiduciary basis, then it is still considered fully effective under IRC §2041(b)(1)(B). As such, it can be presumed that such scheme will also be considered to be effective under the stretch IRA rules.

Language that can assist in ensuring that the power remains fully effective when such individuals are appointed where a power cannot be exercised is as follows:

> *Notwithstanding the above, such power may not be exercised without the written consent of at least two (2) of the five individuals named below, with such approval power being exercisable by any one (1) or more of them without any fiduciary duty to act or not act in any particular manner, provided that if for any reason it is determined that a fiduciary duty exists, then such power shall nevertheless be exercisable, notwithstanding such duty.*

Non-GST Trust Planning

Power of Appointment and stretch trust planning considerations also come about for large estates when assets will be allocated to a "Non- Generation Skipping Trust" for descendants, where the trust assets should be considered as owned by the children of the decedent for federal estate tax purposes to avoid imposition of Federal Generation Skipping Tax on the death of a child. It would be a waste to allocate IRA/Plan or an asset containing "income with respect to a decedent" to the GST share (this applies to all assets if the decedent has insufficient GST exemption).

Most readers know that if an estate exceeds the GST Exemption of a decedent (which is as much as $12,060,000 in 2022) assets to the extent of the GST Exemption amount can pass to a GST Trust that will not be subject to estate tax in the estates of the children of the decedent, and any excess amounts will be held in trust that will be subject to federal estate tax on the death of the children under a "Non-GST Trust" mechanism so as to avoid the imposition of generation skipping transfer tax on a child’s death.

Normally planners will provide the child with a Testamentary Power of Appointment in favor of creditors of the child’s estate under a Non GST Trust in order to cause inclusion of trust assets in the child’s estate to avoid imposition of GST Tax, but when See-Through Trust status was desired to qualify for a lifetime payout before the SECURE Act, there was a question as to whether a Power of Appointment exercisable in favor of "creditors of the estate of the Primary Beneficiary who are people no older than the Primary Beneficiary" would result in loss of the

someone other than one whose interest would be adversely affected by the exercise of the power; an example of someone adversely affected would be a taker-in-default of the exercise of the power)." https://shenkmanlaw.com/uploads/2021/04/Generation-Jumping-Selected-Planning-and-Drafting-Aspects-of-Generation-Skipping-Transfer-Taxation-2.pdf.

ability to stretch payments over the lifetime of the Primary Beneficiary. Under these new Proposed Regulations and the SECURE Act it appears that it will not be problematic to provide for a Power of Appointment held by a Designated Beneficiary (or an Eligible Designated Beneficiary) to be payable to creditors of his or her estate without causing loss of the ability to qualify for a 10-year stretch, or a life expectancy stretch if the power holder is an Eligible Designated Beneficiary and the trust is otherwise properly designed and drafted.

The Ability to Amend, Modify, and Reform

Another aspect of the Proposed Regulations that is taxpayer friendly is that they permit the amendment, modification, and reformation of trusts on or before September 30th of the calendar year following the calendar year of the Plan Participant's death so that trust beneficiaries, creditors, charities, and other entities can be added or removed.[142]

If a trust beneficiary is added after the applicable September 30th date, however, the addition of the new beneficiary will affect the determination of the Designated Beneficiary and therefore the calculation of the Required Minimum Distributions. Additionally, if a beneficiary is added in a calendar year in which a full distribution is not required, and after the addition of such beneficiary full distribution would have been required, the full distribution shall not be required until the end of the calendar year following the calendar year in which the beneficiary was added.

This additional good news from the Proposed Regulations provides the ability to appoint Trust Protectors under a trust document who can have the authority to make changes to the terms of the trust in order to facilitate qualifying for the optimal payout arrangement of Required Minimum Distributions from a IRA/Plan that is made payable to the trust.

The Proposed Regulations allow for such post-death modification to occur within a specified time period following the Plan Participant's death, without causing detrimental effects on the RMD payout period. This can be helpful in allowing planners to obtain the best payout possible for the family, while nevertheless satisfying the See-Through Trust rules.

[142] Previously under § 401(a)(9), the determination of beneficiaries and the resulting Required Minimum Distribution date were determined as of the September 30th Designation Date, but post-death modifications to the trust instrument were not considered to be effective for the purposes of determining the Designated Beneficiary. In other words, beneficiaries' interests were considered as fixed as of the date of the Plan Participant's death, and such beneficiaries could be paid out before the September 30th Designation Date without causing an adverse impact on the Required Minimum Distribution payout. However, under 1.401(a)(9)-4(f)(5)(iii)(B) and (C) "A trust beneficiary . . . may be removed pursuant to a modification of trust terms (such as through a court reformation or a permitted decanting) by September 30 of the calendar year following the calendar year of the employee's death, in which case that person is disregarded in determining the employee's [D]esignated [B]eneficiary . . . A trust beneficiary . . . may be added through a modification of trust terms (such as through a court reformation or a permitted decanting). If the beneficiary is added on or before September 30 of the calendar year following the calendar year of the employee's death, paragraph (c) of this section will apply taking into account the beneficiary that was added. If the beneficiary is added after that September 30, then the rules of paragraph (f)(5)(iv) of this section will apply with respect to the beneficiary that is added."

For example, a Plan Participant establishes an irrevocable trust that provides for the establishment of a See-Through Trust that will receive IRA benefits and provide for the Plan Participant's Surviving Spouse and children (who are over age 21). Under Internal Revenue Code Section 401(a)(9) (and the currently effective Treasury Regulations and Proposed Regulations), the IRA accounts must be completely withdrawn under the 10-Year Rule because the children are not Eligible Designated Beneficiaries (i.e., the five classes of beneficiaries that are eligible for life expectance rule status for Required Minimum Distribution purposes: (1) the Plan Participant's Surviving Spouse; (2) a minor child of the Plan Participant; (3) a disabled beneficiary; (4) a chronically ill beneficiary; and (5) a beneficiary who is not more than 10 years younger than the Plan Participant).

However, if, on or before September 30 of the calendar year following the year of the Plan Participant's death, one or more siblings of the Plan Participant who are less than ten years younger than the Plan Participant are added to the trust to be beneficiaries that are eligible to receive Retirement Plan benefits after the Surviving Spouse's death, and the trust is amended so that distributions cannot be made to the children until after the death of the survivor of the Surviving Spouse and the Plan Participant's sibling, then the Required Minimum Distribution payout period can be based upon the (usually) more favorable life expectancy rule (i.e., where Required Minimum Distributions are to come out over the life expectancy of the oldest trust beneficiary who is eligible to receive benefits from the Retirement Plan).

Specifically the Proposed Regulations read as follows:[143]

(B) Modification of trust to remove trust beneficiaries.

A trust beneficiary described in paragraph (f)(3) of this section may be removed pursuant to a modification of trust terms (such as through a court reformation or a permitted decanting) by September 30 of the calendar year following the calendar year of the employee's death, in which case that person is disregarded in determining the employee's designated beneficiary.

(C) Modification of trust to add trust beneficiaries.

A trust beneficiary described in paragraph (f)(3) of this section may be added through a modification of trust terms (such as through a court reformation or a permitted decanting). If the beneficiary is added on or before September 30 of the calendar year following the calendar year of the employee's death, paragraph (c) of this section will apply taking into account the beneficiary that was added. If the beneficiary is added after that September 30, then the rules of paragraph (f)(5)(iv) of this section will apply with respect to the beneficiary that is added.

To illustrate, consider a revocable trust agreement or a last will and testament that provides for the establishment of a trust that will receive Retirement Plan benefits and provide for the health, education, maintenance and support of the Plan Participant's Surviving Spouse and children (who

[143] Prop. Reg. § 1.401(a)(9)-4(f)(5)(iii), 87 Fed. Reg. 10504 (Feb. 24, 2022).

are over age 21). Under the Proposed Regulations, the Retirement Plan assets must be completely withdrawn under the 10-Year Rule because the children are not Eligible Designated Beneficiaries.

However, the terms of the trust could be modified by the Designation Date to remove the adult children of the Plan Participant from being beneficiaries of the trust so that the life expectancy rule will apply, in lieu of the 10-Year Rule.

If the modification is made after the Designation Date, the Proposed Regulations require the trust to be "retested" to determine which beneficiaries count for the purposes of the Required Minimum Distribution payout period, which could cause a re-determination of the Required Minimum Distribution payout period. This is based upon the following language from the Proposed Regulations:

> (A) Addition of beneficiary after September 30. If, after September 30 of the calendar year following the calendar year of the employee's death, a trust beneficiary described in paragraph (f)(3) of this section is added as a trust beneficiary (whether through the exercise of a power of appointment, the modification of trust terms, or otherwise), then--
>
> (B) The addition of the beneficiary will not cause the trust to fail to satisfy the identifiability requirements of this paragraph (f)(5);
>
> (C) Beginning in the calendar year after the calendar year in which the new trust beneficiary was added, the rules of §1.401(a)(9)-5(f)(1) will apply taking into account the new beneficiary and all of the beneficiaries of the trust that were treated as beneficiaries of the employee before the addition of the new beneficiary; and
>
> (D) Subject to paragraph (f)(5)(v) of this section, the rules of paragraphs (b) and (e)(2) of this section and §1.401(a)(9)-5(f)(2) will apply taking into account the new beneficiary and all of the beneficiaries of the trust that were treated as beneficiaries of the employee before the addition of the new beneficiary.

The removal of a beneficiary after the Designation Date does not affect the Required Minimum Distribution payout period, so it is important to assure that trust agreements are carefully reviewed to help assure that all "undesirable" beneficiaries are removed by the Designation Date.

Absent the exercise of a power of appointment provided under the trust instrument, there are a four ways to accomplish this outcome: (1) Court Reformation, (2) Decanting, (3) Non-Judicial Agreement among the trustee and the trust beneficiaries, and (4) actions by Trust Protectors (or other amendments permitted by the terms of the trust document). The Proposed Regulations treat all of the above mechanisms identically for the purposes of the determination of which beneficiaries of the trust are to be counted in calculating the Required Minimum Distribution payout period.

Court Reformation

A reformation of a trust is the action of modifying the trust instrument through the court system so that it aligns with the intent of the settlor. Four common reasons for a reformation are: (1) scrivener's error; (2) vague or ambiguous language; (3) malpractice error; and (4) change in circumstances not contemplated by the settlor.

A common topic surrounding reformations in wake of the United States Supreme Court case of *Commissioner* v. *Estate of Bosch* 387 U.S. 456 (1967) is whether the IRS will accept and be bound by a court reformation issued by a state court other than the highest court of the applicable State. *Bosch* held that:

> When the application of a federal statute is involved, the decision of a state trial court as to an underlying issue of state law should *a fortiori* not be controlling. . . . If there be no decision by [the State's highest court] then federal authorities must apply what they find to be the state law after giving the "proper regard" to relevant rulings of other courts of the State. In this respect, it may be said to be, in effect, sitting as a state court.

Under the Proposed Regulations, beneficiaries can be added or removed via all of the aforementioned means of modification. However, while post-death modifications are permitted, the Proposed Regulations appear to limit such modifications to the addition or removal of beneficiaries for identifiability purposes and determining which beneficiaries are "countable".

The Proposed Regulations essentially carve out an exception to the *Bosch* holding by stating that state laws governing modification are controlling, at least with respect to the addition or removal of trust beneficiaries for the sole purpose of determining which beneficiaries are "countable" for Required Minimum Distribution payout purposes. This generosity shown by the Treasury should not be construed to apply to post- death modifications to achieve other tax results (such as qualification for the federal estate tax marital deduction).

Similarly, Natalie Choate reminds us of two other tax law precepts that the Proposed Regulations appear to "overrule." First, the IRS has routinely taken the position in court cases and private letter rulings that a post-death trust modification that is made solely for the purpose of reducing tax liability is generally not recognized for tax purposes. Second, the IRS has mentioned in numerous private letter rulings that it would not recognize any post-death trust amendments. These limits do not appear to apply to post-death modifications in relation to determining the "countable" beneficiaries.

Decanting

Decanting is the process of distributing trust assets to a new trust which usually is held for the benefit of the same beneficiaries. Common reasons to decant a trust include asset protection, ease of administration, to correct drafting errors, or to address changes in circumstances that were not contemplated by the settlor when the trust was established. Additionally, before the Designation Date, a trustee could decant a trust to a new improved trust that contains provisions to ensure that the life expectancy rule would apply or to create a more favorable Required Minimum Distribution payout situation that would otherwise apply under the initial trust.

Non-Judicial Modification

Another way to modify the trust agreement without using the court system is through an agreement between the trustee and some or all of the beneficiaries of the trust under a non-judicial modification of trust arrangement, to the extent that this is permitted under applicable state law. Depending upon the terms that are being modified, this form of modification may be difficult due to general requirement of the consent of many if not all of the trust beneficiaries before such an agreement can be effectuated. However, if all parties are on board with a proposed trust modification (and if the modification is not otherwise available through exercise of a power of appointment or trust protector action), then a non-judicial modification can be an effective and less costly method to effectuate a modification of a trust.

While these aforementioned means of modification are viable to amend a trust that has received IRA/Plan benefits to optimize the Required Minimum Distribution payout period, we believe another option to be the most attractive: the use of Trust Protectors.

Trust Protectors

Trust Protectors are one or more individuals who have the power to amend or change a trust agreement to help assure that the settlor's intent is effectuated despite changes in circumstances. Trust Protectors are also used to make changes to limit tax liability in the face of changing laws, and can be granted broad authority to modify an "irrevocable" trust agreement as determined appropriate.

In the aforementioned example, the Trust Protectors could amend the Trust to provide for one or more Eligible Designated Beneficiaries to be potential beneficiaries in an appropriate manner so that the trust can receive IRA/Plan benefits over the life expectancy of the oldest trust beneficiary.

Before the 2000s, the use of Trust Protectors in will and trust drafting was rare, but a good many planners now appropriately offer Trust Protector provisions to their clients to maximize flexibility and convenience for when a trust may need to be changed.

We caution, however, that issues may arise if Trust Protectors are considered to be "fiduciaries" that would have a fiduciary duty to the trust beneficiaries.

Fiduciary or Non-Fiduciary, That is the Question

The classification of a Trust Protector as either a fiduciary or non-fiduciary can have great impact. A fiduciary is someone who must consider, and ultimately act in light of, the best interests of another. In contrast, individuals who do not have a fiduciary duty instead have a "personal" duty. A "personal" duty of care is one that applies the reasonably prudent person standard.

Therefore, if the Trust Protector is deemed to be a "fiduciary" then his or her authority could be confined to acting only in the best interests of the beneficiaries, which can sometimes be contrary with the objective of a contemplated Trust Protector action (particularly if the action would adversely affect one or more beneficiaries' rights under the trust). This can undercut a significant purpose for naming Trust Protectors under a Trust in the first place.

The debate on whether Trust Protectors should be considered fiduciaries or not is ongoing. Essentially, there are two schools of thought: those who believe that Trust Protectors are inherently fiduciaries and those who believe that the provisions of the trust and what powers are granted to Trust Protectors can determine whether they have a fiduciary duty. "Two households, both alike in dignity," the crux of their arguments are provided below.

Notwithstanding this issue, however, as long as Trust Protectors do their job by the Designation Date (September 30 of the calendar year following the calendar year of the death of the Plan Participant) and can cut back their powers as necessary to assure that they have no fiduciary duty to add beneficiaries to any trust receiving Retirement Plan distributions, the question of whether they are fiduciaries should not be an issue, but is interesting to discuss anyway.

Per Se Fiduciary

A preeminent authority on the concept of Trust Protectors, Alexander Bove, summarizes the belief of this school of thought with a single phrase, "a rose will still be a rose, no matter what we call it." Bove's article, *A Protector By Any Other Name….,* addresses the two schools of thought in response to a presentation given by Kathleen Sherby at the 2015 Heckerling Institute on Estate Planning. Sherby's presentation stated that the name given to the position under the terms of the trust would declare the position fiduciary or non-fiduciary.

Bove is not persuaded by the notion that merely changing the "name" of a position can alter the duty held by such position. The root of the issue, he proffers, is the encouragement by legislators for such "sidestepping" of duty by way of the terms of the governing statutes. Legislators have provided that Trust Protectors are fiduciaries or not fiduciaries by default unless the trust expressly states otherwise. The issue Bove has with these statutes is that their terms permit the alteration of the duty of a role, which he claims is inherently fiduciary by nature, by the simple change of the name and inclusion of a statement to that effect in a trust.

The crux of this his argument is that the individuals who hold such a position are called upon to consider the interests of either a beneficiary or the settlor when making their decisions and thus are in fact fiduciaries by their nature, irrespective of their name. Thus, the only way for the Trust Protector to not be a fiduciary is to permit them to act without guidance or instruction. However, practitioners would be unwise to do so as there could be grave consequences and little recourse to be had in the event a Trust Protector acts against the interests of the trust and beneficiaries.

The Terms/Powers Delineated are Determinative

Kathleen Sherby's presentation at the 2015 Heckerling Institute on Estate Planning explained the most effective use of Trust Protectors. Specifically, she argued that the "name" of the position (Trust Protector or Trust Advisor) was determinative of the duties for such role, alongside statutory law for such jurisdiction.

A Trust Advisor is granted powers that are inherently the powers of the trustee and is described in the trust instrument as a fiduciary. A Trust Protector, on the other hand, is a third party granted the authority to make decisions that would otherwise be given to a beneficiary or trustee and is described in the trust instrument as not a fiduciary. Thus, her argument is that the use of the appropriate position title and the indication within the trust instrument of the duty which that title holds is determinative of whether the position has a fiduciary duty or not.

Statutory Law

While differing viewpoints exist on whether the fiduciary/non-fiduciary "labels" bestowed upon Trust Protectors are dispositive, they recognize that statutory law in each jurisdiction ultimately governs. However, the states all vary. Florida, for example, provides that a Trust Protector is by default a fiduciary unless the terms of the trust instrument provide otherwise. In Alaska, on the other hand, the Trust Protector is NOT a fiduciary by default unless the terms of the trust instrument provide otherwise. Other states (such as Virginia) consider Trust Protectors fiduciaries no matter what the trust instrument states.

Our Take

The authors are inclined to support the view that statutory law and even common law, when applicable, can permit drafters of trust instruments to "draft away" any fiduciary duties on the part of Trust Protectors, although nothing is for sure except for death, taxes and James Magner reminding the authors of LISI Newsletter deadlines.

We often offer our clients Trust Protector language and recommend that they consider appointing trusted individuals to act in a non-fiduciary manner with the ability to amend a Trust Agreement for the benefit of the beneficiaries of the Trust. Commonly, the power will only be exercisable with the consent of the settlor's Surviving Spouse or one or more children to help assure that a Trust Protector will not inadvertently or intentionally act in a way that is harmful to the beneficiaries.

Trust documents that we provide for clients also include a "Qualified Plan/IRA Trust Protector" provision which provides an individual with the authority to amend the Trust to optimize the ability to "stretch out" IRA/Plan distributions payable to a Trust.

Nevertheless, the authors are wary of the possible tax consequences if Trust Protectors are considered fiduciaries pursuant to Bove's argument. If Trust Protectors are considered to be fiduciaries and have the authority to add one or more particular individuals as beneficiaries of a trust, then those individuals may be considered "countable" beneficiaries for purposes of the Proposed Regulations, which could adversely affect the Required Minimum Distribution payout period. To avoid this issue, the terms of the provision should be drafted carefully with respect to the description of the position and what powers the Trust Protector is given. Further, use of powers of appointment can achieve similar results, without concerns that the Trust Protectors' potential status as "fiduciaries" could cause detrimental effects on the Required Minimum Distribution payout period for a trust that is the beneficiary of an IRA/Plan.

Nevertheless, given the relatively lenient viewpoint that the IRS has taken under the Proposed Regulations with respect to powers to appointment, it seems that the giving a Trust Protector broad authority to change trust provisions (including the power to add beneficiaries) should not be problematic.

Planners should recommend the inclusion of Trust Protector provisions and the selection of Trust Protectors who can act in a non-fiduciary manner to change the beneficiaries of a trust to comply with the rules in the best way possible for the family.

Time will tell whether the favorable provisions in the Proposed Regulations regarding post-death modification of a trust that is the beneficiary of IRA/Plan assets will continue to apply after the Final Regulations are released, and more specifically, whether the IRS will deem Trust Protectors who have powers to add or remove beneficiaries to be fiduciaries as to such possible future beneficiaries and thus cause an expanded universe of "countable beneficiaries." In the meantime, planners should consider putting carefully drafted Trust Protectors provisions into documents and artfully drafting to permit the use of powers of appointment, at least as to handling trusts that will be the beneficiaries of IRA/Plans to maximize the flexibility (which hopefully will be available once the Proposed Regulations are finalized).

Given the favorable response to this aspect of the Proposed Regulations from planners and commentators alike, it seems unlikely that the Treasury will reverse course on this issue or look unfavorably at Trust Protector provisions in trusts that hold IRA/Plan assets. Nevertheless, there is a chance that we will not know what the rules truly are until the Final Regulations are released and/or until a court interprets them. Until then, prudent planners and taxpayers are best served erring on the side of flexibility and handling each matter as it comes about.

Yet Another Special Surviving Spouse Rule: The Required Minimum Distribution Delay

An often forgotten benefit that is provided to a Surviving Spouse is the ability of a Surviving Spouse to delay the commencement of distributions if the Surviving Spouse is the sole beneficiary, and the Plan Participant did not begin making distributions during their lifetime. As discussed above, in this scenario, the Surviving Spouse is permitted to delay distributions until the end of the calendar year in which the Plan Participant would have attained the age of 72.

If the Surviving Spouse dies prior to the Required Beginning Date, the applicable distribution rules (5-Year, 10-Year, or Stretch) are to be applied as if the Surviving Spouse was the Plan Participant. For this purpose, the date of death of the Surviving Spouse is substituted for that of the Plan Participant.

If the Surviving Spouse remarries and dies prior to the commencement of distributions, the Surviving Spouse's new spouse cannot utilize the delay exception.

This does not apply to spousal rollovers, but the Surviving Spouse may rollover the IRA into his or her own IRA and delay distribution until the Surviving Spouse reaches their own Required Beginning Date.

Conclusion

Although most of the SECURE Act provisions became effective on January 1, 2020, the Proposed Regulations that are contemplated to become effective on January 1, 2022 will be crucial for taxpayers who need to arrange their affairs with respect to qualified plan and IRA benefits going into trusts to safeguard wealth.

At this point, thousands of tax, pension and estate planning advisors are combing through the 275 pages that were recently released and we are all awaiting the Final Regulations. In the meantime, planners and advisors should comply with the Proposed Regulations, monitor the Proposed Regulations' development and future implementation, and relay their findings to clients.

CHAPTER 9 – THE CARES ACT

The CARES Act (the Coronavirus Aid, Relief, and Economic Security Act) that was signed into law on March 27, 2020. The below summarizes the provisions of such Act which related to IRAs and other Qualified Retirement Plans. Mention of the CARES Act also appears throughout this Book where relevant. The SECURE Act is also mentioned throughout the book and extensively in Chapter 7.

The CARES Act implemented the following provisions that related to planning for IRAs and other Qualified Retirement Plans:

1. Required Minimum Distributions Were Waived for All Taxpayers for 2020 (If Not Already Taken)

The CARES Act has eliminated Required Minimum Distributions for most taxpayers for the calendar year 2020. Thus, individuals who were otherwise required to take Required Minimum Distributions from their IRA/Plans may skip taking such distributions in 2020. However, this did not apply to Required Minimum Distributions that are required to be taken from defined benefit plans that are plans established under any of Internal Revenue Code Sections 401, 403, or 457, or from 457 plans that are sponsored by a non-government tax-exempt entity.

The SECURE Act changed the age at which Plan Participants are required to begin taking Required Minimum Distributions to age 72 for anyone turning age 70½ after December 31, 2019. Prior to the SECURE Act becoming effective on January 1, 2020, Required Minimum Distributions generally were required to be taken by individuals who reached age 70½ on or before December 31, 2019. Required Minimum Distributions need to be taken by April 1st of the calendar year following the year in which the individual reaches such age-related threshold. Therefore, individuals who reached age 70 ½ in 2019 and have not yet taken their first Required Minimum Distribution can postpone Required Minimum Distributions for 2019 and 2020.

Delaying such Required Minimum Distribution will allow for a greater amount of time for the IRA/Plan assets to grow tax-free and is even more important with the recent drop in market values. For example, the Dow Jones ended 2019 at over 28,000 but it was at 21,637 on March 27, 2020. If a Required Minimum Distribution was taken before April 1, 2020, the Plan Participant would have to pay ordinary income tax rates on the distribution and would be realizing a lower value. On the other hand, taking the Required Minimum Distribution now could convert ordinary income into capital gains if the markets make a recovery. Plan Participants should take this into consideration when determining whether to take a Required Minimum Distribution.

2. Recontribution Right for 2022 Withdrawals

Individuals who have already taken withdrawals or distributions in 2020 that would have otherwise been Required Minimum Distributions but for the CARES Act will be able to put such withdrawals or distributions back into the IRA/Plan, if: (a) the withdrawal or distribution is recontributed to the IRA/Plan by August 31, 2020;[144] and (b) in the case of a Qualified Retirement Plan, the Plan accepts rollover contributions. The ability to negate a previously taken 2020 Required Minimum Distribution applies to an individual who is considered to be the Plan Participant (including a Surviving Spouse of a deceased Plan Participant who has rolled over the decedent's IRA/Plan into the Surviving Spouse's own IRA), a Surviving Spouse of a deceased Plan Participant who is the beneficiary of an IRA/Plan, or a non-Surviving Spouse beneficiary of an IRA (despite such non-Surviving Spouse beneficiaries not normally being able to effectuate rollovers). Note that a non-Surviving Spouse beneficiary of a non-IRA Qualified Retirement Plan is not entitled to effectuate a rollover to negate the previously taken Required Minimum Distribution, and that the rollover opportunity for such non-Surviving Spouse beneficiaries applies only with respect to an IRA of which he or she is a beneficiary. Further, IRS Notice 2020-51 confirms that any such recontribution will not be considered to be a rollover for the purposes of the "one rollover per 12 month limitation" that is found in Internal Revenue Code Section 408(b)(3)(B). It is not clear whether the Plan Participant or beneficiary must recontribute any specific non-cash item that was distributed, although it seems that this is required (i.e., if non-cash assets are taken as a distribution from the IRA or Qualified Retirement Plan, and are later sold, then any proceeds from the sale thereof could not be recontributed). However, it is clear that only the portion of a distribution taken in 2020 which would have been a Required Minimum Distribution but for the CARES Act's waiver of 2020 Required Minimum Distributions can be rolled back into the IRA/Plan within the extended August 31, 2020 deadline, and that any portion of the distribution that would not have been a Required Minimum Distribution is ineligible for such rollover beyond what is otherwise allowed (i.e., a rollover that is recontributed within 60 days of distribution).

3. IRA Custodian Responsibilities

Notice 2020-51 also provides a robust Questions and Answers section to address "frequently asked questions" emanating from the CARES Act's elimination of the 2020 Required Minimum Distribution requirement. Notably, the Questions and Answers provide that IRA custodians need not amend their documents to have the waiver of 2020 Required Minimum Distributions apply, because such waiver applies automatically. This is welcome news to confirm that all taxpayers are entitled to this benefit, regardless of whether the IRA documents have been amended to provide it. Further, an IRA trustee, issuer or custodian must notify the IRA owner that no Required Minimum Distribution is due for 2020, and this requirement is deemed to be satisfied if a copy of the Form 5498 that is filed with the IRS by such trustee, issuer or custodian is furnished to the IRA owner. The Notice also confirms that the waiver of 2020 Required Minimum Distributions does not apply to a

[144] IRS Notice 2020-51. IRS Notice 2020-23 previously extended the rollover deadline to July 15, 2020, but this has been superseded by IRS Notice 2020-51 which extended the rollover recontribution deadline to August 31, 2020.

Defined Benefit Plan.

4. Confirmation of Required Beginning Date

The Questions and Answers under the Notice also state that an individual's Required Beginning Date does not change, even if such date is April 1, 2020. The deadline by which the taxpayer must take his or her first Required Minimum Distribution is what changes, but his or her Required Beginning Date remains the same. This is important because, if an individual had a Required Beginning Date of April 1, 2020, and dies after April 1, 2020, then he or she is considered to have survived his or her Required Beginning Date, which could affect the Required Minimum Distribution payout options applicable to the beneficiary or beneficiaries of his or her IRA/Plan.

However, an individual who has a Required Beginning Date of April 1, 2021 is obligated to take his or her first Required Minimum Distribution by such date. Under Internal Revenue Code Section 401(a)(9)(I), an individual is required to take a Required Minimum Distribution for the year in which he or she reaches the age of 72 (or is otherwise required to begin taking Required Minimum Distributions, such as if the individual has retired), but the deadline for such first Required Minimum Distribution is the April 1st following the year in which he or she reaches the age of 72 (i.e., his or Required Beginning Date). Because Required Minimum Distributions for 2020 are waived, the deadline for the individual's first Required Minimum Distribution is not until December 31, 2021, and such first Required Minimum Distribution need not include the amount of the Required Minimum Distribution which otherwise would have had to be made for the year 2020. This essentially eliminates the need to decide whether to take the first year's Required Minimum Distribution by December 31, 2020 (i.e., year in which he or she reaches the age of 72 or retires), or to postpone such distribution until April 1 of the next year, since no such Required Minimum Distribution is required for 2020, and allows postponement of the first Required Minimum Distribution until December 31, 2021. This decision is called the "Delay in First Distribution" Decision, and is discussed further in Chapter 2.

5. Deadline to Elect Out of Life Expectancy Rule Into the Five-Year Rule was December 31, 2021 with Respect to Plan Participants who Deceased in 2020

The Notice further clarified that where a Qualified Retirement Plan permits a Plan Participant or a beneficiary to elect to have the 5-Year Rule or the Life Expectancy Rule apply in determining Required Minimum Distributions after the Plan Participant's death, the deadline for making such an election has been extended to December 31, 2021, if the election would otherwise have had to have been made by the end of 2020. This is based upon Treasury Regulation Section 1.401(a)(9)-3, Q&A-4(c), which states that such election must be made by the end of the calendar year following the year of the death of the Plan Participant. However, the changes brought about by the CARES Act are consistent with the treatment of the year 2020 as a "free year" during which no Required Minimum Distributions must be made.

6. Other Important Deadlines Remain Unchanged

The Notice nevertheless points out that several important deadlines remain unchanged by the CARES Act for Plan Participants who died in 2019. Specifically, none of the following important post death deadlines (which are described in further detail in Chapter 3) are extended: (1) the September 30 following the year of death of an IRA owner or Plan Participant on which the Designated Beneficiary is determined for Required Minimum Distribution purposes (the "Designation Date"), (2) the October 31 deadline by which the trustee of a trust that is a Designated Beneficiary of an IRA/Plan's Designated Beneficiary must provide the plan administrator with certain information, or (3) the December 31 deadline by which separate accounts must be established for Required Minimum Distribution Purposes.

7. The "5-Year Rule" Became the "6-Year Rule" When the Year 2020 Is Included

Section 2203 of the CARES Act effectively extended the requirement for certain inherited IRA/Plans that all assets in such an IRA/Plan must be distributed by December 31st of the 5th year following the death of the Plan Participant to now require that such benefits be distributed by December 31st of the sixth year following the Plan Participant's death. This is an increase of one year that applies to IRA/Plans payable where no Designated Beneficiary of the IRA/Plan exists due to the IRA/Plan having been left to a non-individual (such as an estate) or a trust that does not qualify as a "See-Through Trust." The 5-Year Rule applies only where a Plan Participant has died prior to his or her Required Beginning Date and where a lifetime or other "longer stretch" does not apply, and becomes a "6-Year Rule" where the Plan Participant died in 2015 through 2019. This does not affect Plan Participants who die in 2020, as the 5 year period does not begin running until 2021, and therefore is not affected by the suspension of Required Minimum Distributions for 2020.

8. Increased Borrowing from a Pension Plan for 2020

The Act enabled Plan Participants who are harmed by the SARS-CoV-2 coronavirus in certain ways to have 180 days from enactment of the Act (between March 27, 2020 and September 22, 2020) to borrow from pension plans that allow this up to lesser of (a) $100,000 (up from the former $50,000 limit on borrowing); or (b) "the present value of the non-forfeitable accrued benefit of the employee under the plan." The previous law limited this element to being one-half of the present value of the non-forfeitable accrued benefit. If the Plan goes down in value after the loan is made, then the Plan Participant may owe more than the Plan is worth. Loans from IRAs are not permitted, so IRAs are not impacted by this. The amount borrowed under this provision may exceed what is needed to compensate for the economic losses resulting from COVID-19, so long as the individual experiences some adverse financial consequences, as described below.

In order to take advantage of this increased borrowing opportunity, the Plan Participant must be a "Qualified Individual." A Qualified Individual is a person who meets one or more of the following circumstances:[145]

1. He or she experiences adverse financial consequences in 2020 as the result of any of the following five coronavirus-related circumstances:

   A. Being quarantined;

   B. Being furloughed, laid off, or having work hours reduced by an employer;

   C. Being unable to work due to lack of childcare;

   D. Closing or reduced hours of a business owned or operated by the Qualified Individual; or

   E. Other factors as determined by the Secretary of the Treasury (or the Secretary's delegate).

2. The individual, or his or her spouse or dependent, had been diagnosed with SARS-CoV-2 or COVID-19 by a test approved by the Centers for Disease Control and Prevention ("CDC"). It appears that an individual may marry someone with the diagnosis by December 31, 2020 in order to qualify, assuming that the individual does not otherwise qualify under any of the five circumstances mentioned above.

Notice 2020-50 expanded the definition of a "Qualified Individual" to include a person who experiences adverse financial conditions as a result of any one or more of the following:

1. The individual having a reduction in pay (or self-employment income) due to COVID-19 or having a job offer rescinded or start date for a job delayed due to COVID-19;

2. The individual's spouse or a member of the individual's household (as defined below) being quarantined, being furloughed or laid off, or having work hours reduced due to COVID-19, being unable to work due to lack of child care due to COVID-19, having a reduction in pay (or self-employment income) due to COVID-19, or having a job offer rescinded or start date for a job delayed due to COVID-19; or

3. Closing or reducing hours of a business owned or operated by the individual's spouse or a member of the individual's household due to COVID-19.

The Notice states that for purposes of applying these additional factors a member of the

[145] *See* Sec. 2202(a)(4)(A)(i), H.R. 748, CARES Act, 116th Congress (2020).

individual's household is someone who shares the individual's principal residence, but does not provide further guidance with respect to this. Apartment and house sharing advertisements may make mention of the advantages of sharing a residence with a person having one or more of these circumstances, which must be occurring while the circumstances are applicable, or thereafter if the roommates marry.

The plan administrator is entitled to rely upon the Plan Participant's certification that one of the above conditions is satisfied. Nevertheless, the Plan Participant must actually satisfy one of the above conditions in order to take advantage of the increased borrowing opportunity set forth by the CARES Act.

By way of background, Internal Revenue Code §72(p) has for many years required that loans from Pension Plans be fully repaid in equal amortized payments over five years or within a reasonable period of time, if used to purchase a principal residence. Therefore, existing loans that are now being taken which exceed $50,000 by reason of the CARES Act will need to be re-amortized and will provide that payments owed and not already paid in 2020 will be skipped as to both existing and post-Act loans.

Further, Section 2202 of the CARES Act allows for a delayed repayment of monies borrowed from the Plan under this provision by starting the 5-year repayment period on January 1, 2021.[146] Also, any payments that are otherwise due between March 27, 2020 and December 31, 2020 will be delayed for one year, so that two payments would have to be made in the same year.[147] Moreover, the loan will be re-amortized so that the amounts of future payments will be appropriately adjusted to reflect the delayed due date and any interest accruing during such delay.[148]

With reference to the 5-year term of any outstanding loans, the loan maturity date will be pushed back the number of days between and including March 28, 2020 and December 31, 2020 that loans are outstanding. Therefore, the maturity date of all payments due under preexisting loans owed by a qualified individual will be pushed back by up to 279 days (the number of dates between March 28, 2020 and December 31, 2020).

Alternatively, if a qualifying individual took the first loan he or she has ever received from a Pension Plan on June 1, 2020, then the 5-year loan term will be pushed back by 214 days, which is the number of days between June 1, 2020 and December 31, 2020.

Notice 2020-50 provides a safe harbor for payments owed on outstanding loans from Qualified Retirement Plans. Because the CARES Act provides for a delay in outstanding loan payments owed under a loan made from a Qualified Retirement Plan, and for a resulting adjustment in amounts owed due to the delay and accrued interest, guidance was needed to avoid causing a loan to be treated as a distribution under Internal Revenue Code Sections 72(p)(2)(B) and (C) (requiring that Plan loans be repaid within 5 years and for

[146] Sec. 2202(b)(2), H.R. 748, CARES Act, 116th Congress (2020).
[147] Sec. 2202(b)(2)(A), H.R. 748, CARES Act, 116th Congress (2020).
[148] Sec. 2202(b)(2)(B), H.R. 748, CARES Act, 116th Congress (2020).

level amortization of such loans).

The Notice therefore states that a Plan will be treated as satisfying Internal Revenue Code Section 72(p) if a Qualified Individual's obligation to repay a Plan loan is suspended under the Plan for any period beginning not earlier than March 27, 2020, and ending not later than December 31, 2020. Repayments of the loan must resume after December 31, 2020, and the term of the loan may be extended by up to 1 year from the date the loan was originally due to be repaid. If a Plan suspends loan repayments during the above period, the suspension will not cause the loan to be deemed to have been distributed even if, due solely to the suspension, the term of the loan is extended beyond 5 years; however, interest accruing during the such period must be added to the remaining principal of the loan, and the amortization schedule must be adjusted accordingly.

The Notice further states that a Plan satisfies these rules if the loan is re-amortized and repaid in substantially level installments over the remaining period of the loan. This means that a Plan loan could be outstanding for as long as 6 years, so long as the outstanding balance is re-amortized to account for accrued interest and the delay in the payments, which can be a benefit to a great many taxpayers who have had to borrow from their Plans.

9. 2005 Hurricane Katrina Guidance Applied with Respect to Coronavirus-Related Distributions in 2020

Additionally, the IRS released a set of "Frequently Asked Questions" (FAQ) to provide guidance with respect to the increased borrowing from a Qualified Retirement Plan and with respect to Coronavirus-Related Distributions from January 1, 2020, to December 30, 2020 (which are described in Section 11 below).[149] The FAQ does not add significant substantive changes, but provides that the Treasury Department and the IRS anticipate that the guidance on the CARES Act provisions which relate to IRAs and Qualified Retirement Plans will apply the principles of IRS Notice 2005-92 (which was enacted following Hurricane Katrina) to the extent that similar provisions apply. This was confirmed by Notice 2020-50, which followed a similar track as Notice 2005-92, and also added further taxpayer benefits.

Notice 2005-92 allowed certain individuals who were affected by Hurricane Katrina to take "Katrina Distributions" from their IRA/Plans without incurring the 10% excise tax that might otherwise apply under IRS Section 72(t) and also addressed the suspension of the repayment of loans taken against pension plans. The Notice further provided guidance and examples relating to such Katrina Distributions, such as eliminating certain withholding requirements, providing an employer with discretion as to whether to treat distributions as Katrina Distributions from an employer sponsored plan, and allowing a plan sponsor or plan administrator to be entitled to rely on reasonable representations. Moreover, the Notice sets forth examples to provide guidance on filing of tax returns and electing to treat such distributions as recontributions to IRA/Plans.

[149] https://www.irs.gov/newsroom/coronavirus-related-relief-for-retirement-plans-and-iras-questions-and-answers

10. Employer Responsibility With Respect to Coronavirus-Related Distributions in 2020

One notable item brought about by the FAQ is that employers are not required to adopt the distribution and loan rules of Section 2202 of the CARES Act (relating to the increased borrowing and Coronavirus-Related Distributions from January 1, 2020, to December 30, 2020). Nevertheless, a Qualified Individual may treat a distribution that meets the requirements to be a Coronavirus-Related Distribution as Coronavirus-Related Distribution on the individual's federal income tax return. This means that an individual can designate a distribution from his or her Qualified Retirement Plan as a Coronavirus-Related Distribution, despite the employer not treating the distribution as such. This was confirmed by Notice 2020-50, as described below.

Interestingly, the FAQ points out that the CARES Act does not permit a Participant in a Qualified Retirement Plan to take a distribution under the Plan if the terms of the Plan prevent distributions before the occurrence of a certain event. In other words, the CARES Act provides for exceptions only from the 10% excise tax under Internal Revenue Code Section 72(t) but does not grant any rights under the Qualified Retirement Plan that would otherwise be unavailable. Likewise, if a Qualified Retirement Plan does not permit rollovers into the Plan, then no such rollovers are permitted, despite the terms of the CARES Act.

11. Coronavirus-Related Distributions for 2020

Qualified Individuals could also take a "Coronavirus-Related Distribution" of up to \$100,000 in withdrawals of assets from an IRA/Plan between January 1, 2020, and December 30, 2020, without paying the 10% excise tax that normally applies to distributions taken by Plan Participants under age 59½, while having the choice of paying the withdrawn amount back within three years so that this will be treated as if it essentially were a tax-free loan, or having the withdrawal be considered to be taxable income all in 2020, or as taxable income one-third in 2020, one-third in 2021, and one-third in 2022.

IRS Notice 2020-50 provides significant guidance regarding Coronavirus-Related Distributions, and confirms that a Qualified Individual is entitled to designate that a distribution from an IRA/Plan is a Coronavirus-Related Distribution (assuming he or she otherwise qualifies), regardless of whether the Plan treats the distribution as a "Coronavirus-Related Distribution." Therefore, a Distribution that would have been a Required Minimum Distribution, but for the fact that the CARES Act eliminated Required Minimum Distributions for 2020, or where such distribution has been made from a Plan that does not treat the distribution as a Coronavirus-Related Distribution, nevertheless can qualify as a Coronavirus-Related Distribution under the CARES Act. Notice 2020-50 states that a Qualified Individual is permitted to designate any qualifying distribution as a Coronavirus-Related Distribution on the Qualified Individual's timely filed 2020 Form 1040 federal income tax return (including extensions).

Moreover, the Notice 2020-50 indicates that a Qualified Individual need not use Coronavirus-Related Distributions for a need arising from COVID-19 or an adverse financial consequence associated therewith. Accordingly, a Qualified Individual who has experienced adverse financial consequences can receive a Coronavirus-Related Distribution that may greatly exceed the amount or value of the adverse financial consequences that he or she has experienced.

Notice 2020-50 also indicates that the administrator of an eligible retirement plan may rely upon the Plan Participant's certification that he or she is a Qualified Individual in determining whether a distribution is a Coronavirus Related Distribution, unless the administrator has "actual knowledge" to the contrary. The administrator has no duty to inquire as to whether the individual qualifies, unless the administrator possesses sufficiently accurate information to determine the lack of veracity of a certification. A sample certification is provided in Notice 2020-50.

Nevertheless, the individual was only entitled to treat the distribution as a Coronavirus-Related Distribution on his or her federal income tax return if the individual actually meets the eligibility requirements to be considered as a Qualified Individual, regardless of whether the individual provides a duly signed certification to the administrator. The income lost as a result of the required circumstances does not need to equal or exceed the amount of the permitted distribution. For example, a loss of $3,000 in income from the applicable event, or no loss of income if the individual or his or her spouse has contracted the virus and can work from home and have no compensation decrease, will be sufficient to allow for the withdrawal.

While the general rule that monies received as a distribution from a pension or a profit-sharing plan or non-Roth IRA account are taxable, the following advantageous rules apply to Coronavirus-Related Distributions:

A. <u>No 10% Excise Tax.</u> The 10% excise tax that normally applies to distributions made to individuals who have not reached age 59½ will not apply. Internal Revenue Code Section 72(t) generally provides that distributions made before the Qualified Individual turns 59½ will ordinarily be subject to a 10% penalty. This rule does not apply if the withdrawal is a qualified Coronavirus-Related Distribution.

B <u>Can Elect Whether to Recognize all Income Related to the Distribution in 2020 or to Recognize the Income from the Distribution 1/3 in Each of 2020, 2021 and 2022.</u> The taxpayer can treat the entire Coronavirus-Related Distribution as having been received in 2020 as a taxable distribution, which may be the best tax treatment if the taxpayer is in a low bracket or has losses that will make the entire distribution tax-free. Alternatively, the taxpayer may elect to instead allocate the distribution to be considered as having been received one-third in 2020, one-third in 2021, and one-third in 2022.

Notice 2020-50 confirms that the election of whether: (a) to recognize all income associated with the Coronavirus-Related Distribution in 2020; or (b) to recognize income associated with the Coronavirus-Related Distribution one-third in each of

2020, 2021 and 2022, must be made on the Qualified Individual's timely filed 2020 Form 1040 federal income tax return (including extensions), and on a Form 8915-E that is filed with the return. The election must apply consistently to all Coronavirus-Related Distributions received in 2020, so a taxpayer cannot treat one such 2020 Distribution as being taxable one-third in each of 2020, 2021, and 2022, while treating another such Distribution as being fully taxable in 2020 or as a loan. Further, the election is irrevocable once it is made on such timely filed tax return.

C. Recontribute the Distribution Within 3 Years. The Plan Participant may elect to recontribute the Coronavirus-Related Distribution to the IRA/Plan within three years following the distribution, up to the amount received, provided that no recontributions may be made to a Qualified Retirement Plan that does not accept rollovers or recontributions. Internal Revenue Code Section 402(c)(4) was modified by striking 2009 and replacing it with 2020. This means that if an individual takes a Coronavirus-Related Distribution and pays the amounts back within three years, then the distribution will not be considered as having been made from the IRA/Plan. To the extent that such amounts are repaid, such repayments shall be treated as if they were rolled over into a qualified plan via a direct "trustee-to-trustee" transfer within 60 days of the distribution. Characterization as a direct "trustee-to-trustee" rollover means that the rollover does not impact the taxpayer's eligibility for future eligible rollover distributions because the one-every-12-months rule does not apply to trustee-to-trustee transfers.

A recontribution made after 2020 by a Qualified Individual who has received a Coronavirus-Related Distribution in 2020 will result in the need to amend his or her 2020 income tax return, if it has already been filed, and will be expected to result in a refund to be provided to the Qualified Individual if income tax resulting from the Distribution has been paid. In addition to the amended income tax return, the Qualified Individual must file a Form 8915-E with his or her income tax return to report the reduction in gross income by the amount of the recontribution. The Notice states that the Form 8915-E is expected to be available by the end of 2020.

For example, if a Qualified Individual has elected to recognize all income associated with a $50,000 Coronavirus-Related Distribution that she received from her 401(k) in 2020, and later recontributes all $50,000 of such Distribution to the 401(k) after her 2020 federal income tax return is filed, then she will need to file an amended 2020 federal income tax return with a revised Form 8915-E to report a reduction in her gross income by the $50,000 amount and receive a refund.

Where the individual has elected to have the income recognized ratably over 2020, 2021, and 2022, the amount of the recontribution will first reduce the ratable portion of the Coronavirus-Related Distribution that is includable in gross income for the year of repayment. Further, when a recontribution is made to an Eligible Retirement Plan before the filing of the Qualified Individual's federal income tax return for the previous year, then the amount of the recontribution will reduce the ratable portion of the Distribution for that year.

For example, if a Qualified Individual receives a $75,000 Coronavirus-Related Distribution from a 401(k) plan in 2020, elects the 3-year tax deferral treatment on his 2020 federal income tax return, and recontributes $25,000 on April 10, 2022 (which is before his 2021 tax return was due), then the $25,000 recontribution will reduce the 2021 taxable income by $25,000, and the other two (2) years would not be affected.

If the same Qualified Individual had recontributed the $25,000 in December of 2022, then this would reduce the taxable income for 2022, instead of 2021.

Where a recontribution during any of the 3 years exceeds one-third (1/3) of the total amount, then the recontribution first reduces taxable income by one-third (1/3) of the total Coronavirus-Related Distribution for the year of the recontribution, with any excess amount being carried forward or carried back as between the 3-year period, as elected.

For example, if a Qualified Individual receives $90,000 as a Coronavirus-Related Distribution from her IRA in 2020, elects 3-year tax recognition on her timely filed 2020 federal income tax return, and recontributes $40,000 on November 10, 2021 (after her 2020 federal income tax return was due), then assuming that no other recontributions are made, she can elect to do one of the following:

A. Apply $30,000 against income reported on her 2021 federal income tax return, and carry the excess $10,000 forward to reduce taxable income for 2022 (which causes her to recognize only $20,000 of the income associated with the Coronavirus-Related Distribution in 2022); or

B. Apply the $30,000 against 2021 income, in the same way as with option a) above, and carry the excess $10,000 back to reduce taxable income for 2020 by filing an amended 2020 federal income tax return (which reduces her 2020 income associated with the Coronavirus-Related Distribution to $20,000, while not affecting her 2022 income associated with the Coronavirus-Related Distribution).

APPENDIX A-1: IRS TABLES PRIOR TO NEW MORTALITY TABLES HAVING BEEN RELEASED

TABLE A-1 – UNIFORM LIFETIME TABLE

TABLE III
(Uniform Lifetime)

For Use by:

- **Unmarried Owners,**
- **Married Owners Whose Spouses Are Not More Than 10 Years Young, and**
- **Married Owners Whose Spouses Are Not the Sole Beneficiaries of Their IRA/Plan**

Age	Distribution Period	Age	Distribution Period
70	27.4	93	9.6
71	26.5	94	9.1
72	25.6	95	8.6
73	24.7	96	8.1
74	23.8	97	7.6
75	22.9	98	7.1
76	22.0	99	6.7
77	21.2	100	6.3
78	20.3	101	5.9
79	19.5	102	5.5
80	18.7	103	5.2
81	17.9	104	4.9
82	17.1	105	4.5
83	16.3	106	4.2
84	15.5	107	3.9
85	14.8	108	3.7
86	14.1	109	3.4
87	13.4	110	3.1
88	12.7	111	2.9
89	12.0	112	2.6
90	11.4	113	2.4
91	10.8	114	2.1
92	10.2	115 and over	1.9

TABLE B-1 – JOINT AND LAST SURVIVOR TABLE

TABLE II (continued) (Joint Life and Last Survivor Expectancy) (For Use by Owners Whose Spouses Are More Than 10 Years Younger and Are the Sole Beneficiaries of Their IRA/Plan)										
AGES	**60**	**61**	**62**	**63**	**64**	**65**	**66**	**67**	**68**	**69**
76	26.3	25.6	24.8	24.1	23.4	22.7	22.0	21.4	20.8	20.2
77	26.2	25.4	24.7	23.9	23.2	22.5	21.8	21.2	20.6	19.9
78	26.1	25.3	24.6	23.8	23.1	22.4	21.7	21.0	20.3	19.7
79	26.0	25.2	24.4	23.7	22.9	22.2	21.5	20.8	20.1	19.5
80	25.9	25.1	24.3	23.6	22.8	22.1	21.3	20.6	20.0	19.3
81	25.8	25.0	24.2	23.4	22.7	21.9	21.2	20.5	19.8	19.1
82	25.8	24.9	24.1	23.4	22.6	21.8	21.1	20.4	19.7	19.0
83	25.7	24.9	24.1	23.3	22.5	21.7	21.0	20.2	19.5	18.8
84	25.6	24.8	24.0	23.2	22.4	21.6	20.9	20.1	19.4	18.7
85	25.6	24.8	23.9	23.1	22.3	21.6	20.8	20.1	19.3	18.6
86	25.5	24.7	23.9	23.1	22.3	21.5	20.7	20.0	19.2	18.5
87	25.5	24.7	23.8	23.0	22.2	21.4	20.7	19.9	19.2	18.4
88	25.5	24.6	23.8	23.0	22.2	21.4	20.6	19.8	19.1	18.3
89	25.4	24.6	23.8	22.9	22.1	21.3	20.5	19.8	19.0	18.3
90	25.4	24.6	23.7	22.9	22.1	21.3	20.5	19.7	19.0	18.2
91	25.4	24.5	23.7	22.9	22.1	21.2	20.5	19.7	18.9	18.2
92	25.4	24.5	23.7	22.9	22.0	21.2	20.4	19.6	18.9	18.1
93	25.4	24.5	23.7	22.8	22.0	21.2	20.4	19.6	18.8	18.1
94	25.4	24.5	23.6	22.8	22.0	21.1	20.4	19.6	18.8	18.0
95	25.3	24.5	23.6	22.8	22.0	21.1	20.3	19.6	18.8	18.0
96	25.3	24.5	23.6	22.8	21.9	21.1	20.3	19.5	18.8	18.0
97	25.3	24.5	23.6	22.8	21.9	21.1	20.3	19.5	18.8	18.0
98	25.3	24.4	23.6	22.8	21.9	21.1	20.3	19.5	18.7	17.9
99	25.3	24.4	23.6	22.7	21.9	21.1	20.3	19.5	18.7	17.9
100	25.3	24.4	23.6	22.7	21.9	21.1	20.3	19.5	18.7	17.9
101	25.3	24.4	23.6	22.7	21.9	21.1	20.2	19.4	18.7	17.9
102	25.3	24.4	23.6	22.7	21.9	21.0	20.2	19.4	18.7	17.9
103	25.3	24.4	23.6	22.7	21.9	21.0	20.2	19.4	18.6	17.9
104	25.3	24.4	23.5	22.7	21.9	21.0	20.2	19.4	18.6	17.8
105	25.3	24.4	23.5	22.7	21.9	21.0	20.2	19.4	18.6	17.8
106	25.3	24.4	23.5	22.7	21.9	21.0	20.2	19.4	18.6	17.8
107	25.2	24.4	23.5	22.7	21.8	21.0	20.2	19.4	18.6	17.8
108	25.2	24.4	23.5	22.7	21.8	21.0	20.2	19.4	18.6	17.8
109	25.2	24.4	23.5	22.7	21.8	21.0	20.2	19.4	18.6	17.8
110	25.2	24.4	23.5	22.7	21.8	21.0	20.2	19.4	18.6	17.8
111	25.2	24.4	23.5	22.7	21.8	21.0	20.2	19.4	18.6	17.8
112	25.2	24.4	23.5	22.7	21.8	21.0	20.2	19.4	18.6	17.8
113	25.2	24.4	23.5	22.7	21.8	21.0	20.2	19.4	18.6	17.8
114	25.2	24.4	23.5	22.7	21.8	21.0	20.2	19.4	18.6	17.8
115+	25.2	24.4	23.5	22.7	21.8	21.0	20.2	19.4	18.6	17.8

TABLE C-1– SINGLE LIFE TABLE

TABLE I (Single Life Expectancy)			
AGE	Life Expectancy	Age	Life Expectancy
0	82.4	28	55.3
1	81.6	29	54.3
2	80.6	30	53.3
3	79.7	31	52.4
4	78.7	32	51.4
5	77.7	33	50.4
6	76.7	34	49.4
7	75.8	35	48.5
8	74.8	36	47.5
9	73.8	37	46.5
10	72.8	38	45.6
11	71.8	39	44.6
12	70.8	40	43.6
13	69.9	41	42.7
14	68.9	42	41.7
15	67.9	43	40.7
16	66.9	44	39.8
17	66.0	45	38.8
18	65.0	46	37.9
19	64.0	47	37.0
20	63.0	48	36.0
21	62.1	49	35.1
22	61.1	50	34.2
23	60.1	51	33.3
24	59.1	52	32.3
25	58.2	53	31.4
26	57.2	54	30.5
27	56.2	55	29.6

APPENDIX A-2: IRS TABLES APPLICABLE TO DISTRIBUTION CALENDAR YEARS BEGINNING ON OR AFTER JANUARY 1, 2022

TABLE A-2 – UNIFORM LIFETIME TABLE

TABLE III
(Uniform Lifetime)

For Use by:

- **Unmarried Owners,**
- **Married Owners Whose Spouses Are Not More Than 10 Years Young, and**
- **Married Owners Whose Spouses Are Not the Sole Beneficiaries of Their IRA/Plan**

Age	Distribution Period	Age	Distribution Period
72	27.4	97	7.8
73	26.5	98	7.3
74	25.5	99	6.8
75	24.6	100	6.4
76	23.7	101	6.0
77	22.9	102	5.6
78	22.0	103	5.2
79	21.1	104	4.9
80	20.2	105	4.6
81	19.4	106	4.3
82	18.5	107	4.1
83	17.7	108	3.9
84	16.8	109	3.7
85	16.0	110	3.5
86	15.2	111	3.4
87	14.4	112	3.3
88	13.7	113	3.1
89	12.9	114	3.0
90	12.2	115	2.9
91	11.5	116	2.8
92	10.8	117	2.7
93	10.1	118	2.5
94	9.5	119	2.3
95	8.9	120 and over	2.0
96	8.4		

TABLE B-2 – JOINT AND LAST SURVIVOR TABLE

TABLE II (continued) (Joint Life and Last Survivor Expectancy)
(For Use by Owners Whose Spouses Are More Than
10 Years Younger and Are the Sole Beneficiaries of Their IRA/Plan)

AGES	60	61	62	63	64	65	66	67	68	69
76	28.2	27.4	26.6	25.9	25.2	24.4	23.7	23.1	22.4	21.8
77	28.0	27.3	26.5	25.7	25.0	24.3	23.5	22.9	22.2	21.5
78	27.9	27.1	26.4	25.6	24.8	24.1	23.4	22.7	22.0	21.3
79	27.8	27.0	26.2	25.5	24.7	23.9	23.2	22.5	21.8	21.1
80	27.8	26.9	26.1	25.3	24.6	23.8	23.1	22.3	21.6	20.9
81	27.7	26.9	26.0	25.2	24.5	23.7	22.9	22.2	21.5	20.7
82	27.6	26.8	26.0	25.2	24.4	23.6	22.8	22.1	21.3	20.6
83	27.5	26.7	25.9	25.1	24.3	23.5	22.7	22.0	21.2	20.5
84	27.5	26.7	25.8	25.0	24.2	23.4	22.6	21.9	21.1	20.4
85	27.4	26.6	25.8	25.0	24.1	23.3	22.6	21.8	21.0	20.3
86	27.4	26.6	25.7	24.9	24.1	23.3	22.5	21.7	20.9	20.2
87	27.4	26.5	25.7	24.9	24.0	23.2	22.4	21.6	20.9	20.1
88	27.3	26.5	25.6	24.8	24.0	23.2	22.4	21.6	20.8	20.0
89	27.3	26.4	25.6	24.8	24.0	23.1	22.3	21.5	20.7	20.0
90	27.3	26.4	25.6	24.7	23.9	23.1	22.3	21.5	20.7	19.9
91	27.3	26.4	25.6	24.7	23.9	23.1	22.3	21.5	20.7	19.9
92	27.2	26.4	25.5	24.7	23.9	23.0	22.2	21.4	20.6	19.8
93	27.2	26.4	25.5	24.7	23.8	23.0	22.2	21.4	20.6	19.8
94	27.2	26.3	25.5	24.7	23.8	23.0	22.2	21.4	20.6	19.8
95	27.2	26.3	25.5	24.6	23.8	23.0	22.2	21.4	20.6	19.7
96	27.2	26.3	25.5	24.6	23.8	23.0	22.2	21.3	20.5	19.7
97	27.2	26.3	25.5	24.6	23.8	23.0	22.1	21.3	20.5	19.7
98	27.2	26.3	25.5	24.6	23.8	22.9	22.1	21.3	20.5	19.7
99	27.2	26.3	25.4	24.6	23.8	22.9	22.1	21.3	20.5	19.7
100	27.1	26.3	25.4	24.6	23.8	22.9	22.1	21.3	20.5	19.7
101	27.1	26.3	25.4	24.6	23.8	22.9	22.1	21.3	20.5	19.7
102	27.1	26.3	25.4	24.6	23.7	22.9	22.1	21.3	20.5	19.7
103	27.1	26.3	25.4	24.6	23.7	22.9	22.1	21.3	20.5	19.6
104	27.1	26.3	25.4	24.6	23.7	22.9	22.1	21.3	20.5	19.6
105	27.1	26.3	25.4	24.6	23.7	22.9	22.1	21.3	20.5	19.6
106	27.1	26.3	25.4	24.6	23.7	22.9	22.1	21.3	20.5	19.6
107	27.1	26.3	25.4	24.6	23.7	22.9	22.1	21.3	20.5	19.6
108	27.1	26.3	25.4	24.6	23.7	22.9	22.1	21.3	20.5	19.6
109	27.1	26.3	25.4	24.6	23.7	22.9	22.1	21.3	20.4	19.6
110	27.1	26.3	25.4	24.6	23.7	22.9	22.1	21.3	20.4	19.6
111	27.1	26.3	25.4	24.6	23.7	22.9	22.1	21.3	20.4	19.6
112	27.1	26.3	25.4	24.6	23.7	22.9	22.1	21.3	20.4	19.6
113	27.1	26.3	25.4	24.6	23.7	22.9	22.1	21.3	20.4	19.6
114	27.1	26.3	25.4	24.6	23.7	22.9	22.1	21.3	20.4	19.6
115	27.1	26.3	25.4	24.6	23.7	22.9	22.1	21.3	20.4	19.6
116	27.1	26.3	25.4	24.6	23.7	22.9	22.1	21.3	20.4	19.6
117	27.1	26.3	25.4	24.6	23.7	22.9	22.1	21.2	20.4	19.6
118	27.1	26.3	25.4	24.5	23.7	22.9	22.1	21.2	20.4	19.6
119	27.1	26.2	25.4	24.5	23.7	22.9	22.1	21.2	20.4	19.6
120+	27.1	26.2	25.4	24.5	23.7	22.9	22.0	21.2	20.4	19.6

TABLE C-2 – SINGLE LIFE TABLE

TABLE I (Single Life Expectancy)			
AGE	Life Expectancy	Age	Life Expectancy
0	84.6	30	55.3
1	83.7	31	54.4
2	82.8	32	53.4
3	81.8	33	52.5
4	80.8	34	51.5
5	79.8	35	50.5
6	78.8	36	49.6
7	77.9	37	48.6
8	76.9	38	47.7
9	75.9	39	46.7
10	74.9	40	45.7
11	73.9	41	44.8
12	72.9	42	43.8
13	71.9	43	42.9
14	70.9	44	41.9
15	69.9	45	41.0
16	69.0	46	40.0
17	68.0	47	39.0
18	67.0	48	38.1
19	66.0	49	37.1
20	65.0	50	36.2
21	64.1	51	35.3
22	63.1	52	34.3
23	62.1	53	33.4
24	61.1	54	32.5
25	60.2	55	31.6
26	59.2	56	30.6
27	58.2	57	29.8
28	57.3	58	28.9
29	56.3	59	28.0

APPENDIX B: FORMS

SAMPLE PROVISIONS FOR OPERATING AGREEMENT OF LLC OWNED UNDER IRA

IRS APPROVED FINANCIAL INSTITUTION TO OWN LLC THAT WILL INVEST IN REAL ESTATE AND NOT ENTER INTO ANY TRANSACTION OR RELATIONSHIP WITH IRA PARTICIPANT OR FAMILY MEMBERS:

* * * * * * *

AMENDED AND RESTATED OPERATING AGREEMENT OF AMERICAN DREAM, L.L.C.,

A FLORIDA LIMITED LIABILITY COMPANY

WHEREAS, the Company was formed for the sole purpose of being held under the above referenced IRA by the Member, and to be conducted pursuant to the rules that apply to such arrangements.

WHEREAS, the parties are willing to follow such rules, and to enter into this Operating Agreement.

NOW, THEREFORE, for good and valuable consideration, receipt of which is hereby acknowledged, and the mutual promises contained herein, the parties hereto agree as follows:

* * * * * * *

1.09 The term “Prohibited Transaction” shall mean any transaction that would constitute a prohibited transaction under Internal Revenue Code Section 4975.

1.10 The Manager, and any Family Member of the Manager, shall be considered a “Disqualified Person” for all purposes under this Agreement.

1.11 The term “Family Member” shall be considered to include any spouse, ancestor, lineal descendant, and any spouse of a lineal descendant of any Manager or any IRA owner.

* * * * * * *

2.03 **Purpose of Company**. The purpose of the Company is to engage in any and lawful business activities permitted under applicable law, but only to the extent permitted with respect to a limited liability company owned under an Individual Retirement Account, and for all purposes the authority, powers, and immunities provided under this Agreement shall be limited to those that are permitted for an Individual Retirement Account owned limited liability company. Under no circumstances shall there be any Member of this Company other than the applicable Individual Retirement Account without unanimous consent of all Members, which must be granted in writing, in advance, and may be withheld in the absolute discretion of Member. No Manager shall commit a Prohibited Transaction or allow the Company to own any interest in any business, enterprise, or other entity that would generate Unrelated Business Taxable Income as defined and applicable under Internal Revenue Code Sections 511 through 514.

* * * * * * *

5.14 The Section 2.03 shall apply notwithstanding any other provision herein to the contrary.

* * * * * * *

ARTICLE THREE - NAME AND PLACE OF BUSINESS

3.01 **Name of Limited Liability Company**. The name of the Company shall be AMERICAN DREAM, L.L.C. The business of the Company shall be conducted under this name and under any variations of this name that may be necessary to comply with applicable laws and practices of other states within which the Company may do business or make investments.

3.02 **Name of Member**. The name of the Member of this Company is as follows:

FINANCIAL INSTITUTION DULY QUALIFIED AS IRA CUSTODIAN FBO (FOR THE BENEFIT OF) JOHN Q. TAXPAYER IRA

* * * * * * *

8.06 **Entity Classification Election**. The Member intends that the Company shall be a disregarded entity for federal income tax purposes. Therefore, it is not intended that any notice will be filed with the Internal Revenue Service to have this LLC treated as a partnership or a corporation for federal tax purposes, and this Operating Agreement shall be construed and administered accordingly, notwithstanding any provision herein to the contrary.

* * * * * * *

9.02 **Control and Management**. The Company shall be managed by its Manager as described in the Articles of Organization of the Company and Section 9.01 above. The Manager shall be elected and may be replaced from time to time by the majority in interest of the Members. Except as otherwise set forth herein, the Manager shall have sole and exclusive right to manage the business of the Company, subject to the limitations set forth herein, including those limitations described in Section 2.03 hereof. Subject to any limitations expressly set forth in this Operating Agreement, the Manager shall have the authority to take whatever actions the Manager deems appropriate in connection with the management and conduct of the business and affairs of the Company, including, but not limited to, the following:

9.03 **Compensation**. The Manager or Managers shall not be entitled to receive compensation for acting as Manager unless otherwise agreed by the unanimous consent of the Members, but shall be entitled to reimbursement for reasonable expenses paid by the Manager or Managers arising out of the business of the Company. Such compensation and reimbursement may be paid as incurred or in arrears with interest at the predominant prime rate as reported in the Wall Street Journal from time to time.

9.04 **Arm's-Length**. Manager and Company shall remain in an arm's-length relationship, and under no circumstances will there be any transaction, payment, obligation, or understanding that would violate the rules associated with the management of a limited liability company owned by an Individual Retirement Account or a Prohibited Transaction.

* * * * * * *

ARTICLE ELEVEN - PROHIBITED ACTIONS

11.01 **Prohibited Actions**. During the time of the organization or continuance of the Company, no Member or Manager shall do any of the following:

(a) Use the name of the Company (or substantially similar name) or any trademark or trade name adopted by the Company, except in the ordinary course of the Company business;

(b) Disclose to any non-Member any of the Company business practices, trade secrets, or any other information not generally known to the business community;

(c) Do any other act or deed with the intention of harming the business operations of the Company;

(d) Do any act in contravention of this Operating Agreement, except with the prior written consent of the majority in interest of all of the Members;

(e) Do any act which would make it impossible to carry on the intended or ordinary business of the Company;

(f) Confess a judgment against the Company;

(g) Possess Company property or assign the rights of the Company in specific Company property for other than Company purposes; and

(h) Enter into a Prohibited Transaction with the Company or with respect to the Company or the Individual Retirement Account that is the owner of the Company.

11.02 **Use of Company Assets**. No Manager or Member shall use, directly or indirectly, the assets of the Company for any purpose other than carrying on the business of the Company for the full and exclusive benefit of the Company and all of its Members unless fair value is paid for such usage.

* * * * * * *

15.19 **Legal Representation**. The parties acknowledge that this Operating Agreement and the corporate documents for the Company were drafted by GASSMAN, CROTTY AND DENICOLO, P.A. at the request of the Manager, and that the Members have had the opportunity to seek independent legal counsel and have done so or have waived such opportunity. The parties acknowledge that under the applicable Florida Bar Rules information provided to GASSMAN, CROTTY AND DENICOLO, P.A. relating to the subject matter of this Agreement will be accessible to all Managers, Officers and Directors of the Company, and that in the event of a "conflict" between parties associated with this arrangement, GASSMAN, CROTTY AND DENICOLO, P.A. may be required by applicable Florida Bar Rules to withdraw from further representing one or more of the parties hereto or the Company itself. Further, the parties have not relied upon any tax advice from GASSMAN, CROTTY AND DENICOLO, P.A., and have agreed to procure independent legal and tax advice with respect to any and all conduct of the Company.

* * * * * * *

IN WITNESS WHEREOF, each party has executed this Amended and Restated Operating Agreement or a counterpart hereof on the _______ day of ____________________, 20______.

The undersigned Manager and Member hereby execute and agree to be bound by the terms of this Amended and Restated Operating Agreement for AMERICAN DREAM, L.L.C., a copy of which has been delivered to the undersigned.

MANAGER:

JOHN Q. TAXPAYER'S WIFE

MEMBER:

FINANCIAL INSTITUTION DUALLY QUALIFIED AS IRA CUSTODIAN FBO (FOR THE BENEFIT OF) JOHN Q. TAXPAYER IRA

____

By: (Print Name) ____________________
Its: ______________________________

SAMPLE LANGUAGE FOR PROGRAMMING FOR TAX EFFICIENCY BETWEEN GST AND NON-GST TRUSTS

I have or intend to make my children, SON SMITH, and DAUGHTER SMITH, the direct beneficiaries of my IRA account or accounts, and any other pension, 403(b), defined contribution, defined benefit, 401(k), and other Qualified Retirement Plan accounts that I own ("IRA and Plan Accounts"). I have provided or intend to provide that if a said child of mine does not survive me, then the account or portion of the account that would have passed to such child shall pass to this Trust Agreement. If a child does not survive me and his or her share of such IRA and Plan accounts are therefore payable to this Trust, such benefits and/or beneficiary rights shall be divided equally between the surviving children of such predeceased child, per stirpes, and allocated to the separate trusts established for such descendants, being first to the non-generation skipping trust shares established under Section 4.02(c) to the extent that the amount of such IRA and Plan Account exceed the maximum amount of such benefits that can be funded into the generation skipping trust shares, it being my intention that each grandchild of mine shall be the "Designated Beneficiary" for IRA and Plan Account minimum distribution rules in the event that one or both of my said children predecease me, and second to the generation skipping trust shares established under Section 4.02(b), if and to the extent funded.

If a child does not survive me and leaves no descendants, then the IRA and Plan Account share of such child shall be devised with the remaining assets under this Trust passing to the other child and/ or to the descendants of the other child on a per stirpes basis, which would presently result in the share of SON SMITH passing first to the non-generation skipping trust established for DAUGHTER SMITH (or her descendants if DAUGHTER SMITH does not survive SON SMITH) to the extent funded, and then to the generation skipping trust established for DAUGHTER SMITH (or her descendants, if she does not survive SON SMITH), due to SON SMITH not having descendants.

Notwithstanding anything to the contrary above, in the event that any Roth IRAs are payable to this Trust Agreement, then such Roth IRAs shall be allocated first to the generation skipping trust shares established under Section 4.02(b), and then to the non-generation skipping trust shares established under Section 4.02(c), to the extent that the amount of such Roth IRAs exceed the maximum amount of such benefits that can be funded into the generation skipping trust shares.

SAMPLE LANGUAGE FOR CHARITABLE FOUNDATION UNDER ESTATE OR TRUST TO RECEIVE IRA DISTRIBUTION

(c) CHARITABLE FOUNDATION FOR __________________________. I intend to make $1,000,000 payable by IRA beneficiary designation to establish a ____________________ Charitable Foundation for __________________________________ upon my death. My son, JOHN SMITH and MARY DOE, CPA, shall serve the federal estate tax charitable deduction as an Internal Revenue Code Section 501(c)(3) organization. The purpose of that organization will be ____. I specifically authorize that any income of such trust and/or IRA benefits, or income in respect of decedent from the above referenced IRA benefits or otherwise, be payable to the applicable charitable trust and/or estate be entitled to the income tax charitable deduction with respect to the devise to the above referenced charitable trust and/or the charities designated thereunder. The trust agreement to be executed after my death to fulfill the requirements of this disposition shall include the following language, which will apply notwithstanding any language under this Agreement to the contrary:

A. This trust is created to devote and apply the trust assets exclusively for charitable and educational purposes, either by conducting direct charitable and educational activities or by making contributions to organizations duly authorized to carry on such activities and which have established their tax-exempt status under the provisions of Section 501(c)(3) of the Code, and its regulations as they now exist or may hereafter be amended, or by contributions to foreign organizations duly authorized to carry on such activities and as to which the trustees have made a good faith determination utilizing reasonable judgment that the distribution to the organization would be treated as a distribution to an organization described in Section 501(c)(3) and the property, assets, and net income of this trust are irrevocably dedicated to such purposes, with all of such distributions, actions, and endeavors to be consistent with and limited by those activities and expenditures which are permitted to facilitate qualification for tax exempt status under the provisions of Section 501(c)(3) of the Code, and its regulations as they now exist or may hereafter be amended.

B. Notwithstanding any other provision contained in this trust agreement, the trust shall be subject to each and all of the following limitations and restrictions:

1. *Legislative or Political Activities.* None of the activities of this trust shall consist of the carrying on of propaganda, or otherwise attempting, to influence legislation, nor shall this trust participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office.

2. *No Private Benefit*. No part of the net earnings of this trust shall inure to the benefit of any private individual having a personal or private interest in the

activities of the trust, within the meaning of Section 501(c)(3) of the Code and its regulations, as they now exist or may hereafter be amended.

3. *Distribution of Income*. Notwithstanding any other provision contained herein, the Trustees shall distribute the income of this trust for each taxable year at such time and in such manner as not to become subject to the tax on undistributed income imposed by Section 4942 of the Code, during any year in which the trust would be subject to the tax on undistributed income imposed by Section 4942 of the Code.

4. *Prohibited Transactions*. Notwithstanding any other provision contained herein, the Trustees shall not engage in any act of self-dealing as defined in Internal Revenue Code Section 4941(d); nor retain any excess business holding as defined in Internal Revenue Code Section 4943(c); nor make any investments in such manner as to incur tax liability under Internal Revenue Code Section 4944; nor make any taxable expenditures as defined in Internal Revenue Code Section 4945(d).

C. <u>Charitable Distributions</u>. The Trustees appointed under this trust shall hold the Trust property, shall invest and reinvest said property, and shall make distributions in one or more of the following ways: (a) directly for charitable purposes within the meaning of Internal Revenue Code Section 501(c)(3) so that such distributions are “qualified distributions” within the meaning of Internal Revenue Code Section 4942(g) and the corresponding regulations, and/or (b) to charitable organizations described in Section 4.02(c) of this Trust Agreement (being the RESTATED AND AMENDED LIVING TRUST). The trustees may distribute the trust fund, either as to principal or income or both, as they may in their judgment deem most conducive to the public welfare. Subject to the requirement of annual distributions of income under Section 4.01(c) hereof, it has been recommended, but is not required, that substantially all of the lesser of the trust’s adjusted net income or minimum investment return as defined in Internal Revenue Code Section 4942(e)(1), be expended annually for active charitable purposes from the income of the trust and if such income is then insufficient from the principal and available income. It is further recommended, although not required, that the trust be operated in such a manner so that the Trust qualifies as a “private operating foundation” within the meaning of the Code.

D. <u>Termination of Trust</u>. Upon termination of this trust for any reason, the Trustees shall distribute the remaining net assets of the trust estate, including principal and accumulated income, outright and free of trust to one or more organizations which themselves are exempt as organizations described in Internal Revenue Code Section 501(c)(3) and Internal Revenue Code Section 170(c)(2), or to the federal, state, or local government for exclusive public purposes.

E. Compensation and Trustees. Any licensed trust company serving as Trustee shall be entitled to receive as compensation for its services as Trustee the fees it normally charges to similar trusts under its regularly published fee schedule as the same may, from time to time, be amended. Any individual serving as Trustee may receive reasonable compensation. The Trustees shall have the right to be reimbursed for any out-of-pocket expenses associated with this trust, including, but not limited to, brokerage commissions, attorney, real estate management and tax preparation fees, and other extraordinary expenses. It will be permissible to have family members compensated for services rendered, at reasonable hourly rates where the family member is dedicated to the cause of the foundation and provides appropriate documentation and confirmation of services actually rendered, subject to the requirements of applicable Internal Revenue Code regulation and other rules that may limit the hiring of family and the compensation to be paid to family.

APPENDIX C - BOBROW RAISES BROWS

BY ALAN GASSMAN AND BRANDON KETRON

The Required Minimum Distribution rule expert community was shaken by the January 28, 2014 Tax Court Memorandum decision of *Bobrow v. Commissioner*. [150]

While this decision is not binding precedence as an un-reviewed Tax Court Memorandum, members of the tax community feel that Mr. Bobrow, who is a tax lawyer in New York, was treated inappropriately when he had followed IRS Publication 590 and a Proposed Regulation by taking what he thought would be a tax free rollover from one IRA to the other. Internal Revenue Code Section 408(d)(3)(B) provides that there can be only one tax free rollover by an individual within a twelve month period, but Publication 590 and a Proposed Regulation had provided that a second tax free distribution would be permitted if it came from an IRA account that was not drawn upon in the earlier distribution. The Tax Court found that the IRS's interpretation conflicted with the statute, and "overruled" the Publication in holding that a second roll over was not allowed.

This brings up the question as to whether it is safe to follow any regulatory provision not specifically set forth under Internal Revenue Code Section 401(a)(9), finalized Treasury Regulations, or IRS acquiesced without obtaining a Private Letter Ruling.

NOTE - Mr. Bobrow ended up paying the 10% early withdrawal excise tax and was also subject to the 20% penalty for the substantial understatement of income tax. This decision strengthens the suggestion that cautious taxpayers should file a Form 5498 (see below) and at a minimum fill in the applicable sections each year to get the three year statute of limitations on review running, particularly if they have relied upon IRS regulations that go beyond what Internal Revenue Code Section401(a)(9) explicitly permits.

Notable situations where the invalidation of Treasury Regulations would have a significant material negative impact in the minimum distribution rules arena include the following:

I. <u>Ten Year Younger Spouse Assumption Would No Longer Apply</u>. A living participant having reached the Required Beginning Date is able to calculate minimum distributions as if married to someone ten years younger (unless actually married to someone more than ten years younger). A literal reading of Internal Revenue Code Section 401(a)(9)(A)(ii) would require use of the actual joint life expectancy of the participant and the participant's actual spouse (not a spouse ten years younger), or just the participant alone if not actually married.

II. <u>5-Year Rule Choice Would Not Apply When the Deceased Participant Dies Before Required Beginning Date.</u> When a participant has died before his Required Beginning Date, the regulations allow the Designated Beneficiary to choose between taking life expectancy payments over his or her lifetime or waiting until on or before the December 31st of the 5th calendar year

[150] 10 *Bobrow v. Comm'r,* TC Memo 2014-21 (1/28/14).

ending after the date of death of the participant before taking any distributions whatsoever. The Code provides that the 5-Year Rule would apply only if there is no Designated Beneficiary.

APPENDIX D–FORM 5329

Form **5329** (Rev. January 2020) Department of the Treasury Internal Revenue Service (99)

Additional Taxes on Qualified Plans (Including IRAs) and Other Tax-Favored Accounts

▶ Attach to Form 1040, 1040-SR, or 1040-NR.

▶ Go to *www.irs.gov/Form5329* for instructions and the latest information.

OMB No. 1545-0074 | 2019 | Attachment Sequence No. 29

Name of individual subject to additional tax. If married filing jointly, see instructions. | Your social security number

Fill in Your Address Only if You Are Filing This Form by Itself and Not With Your Tax Return ▶

Home address (number and street), or P.O. box if mail is not delivered to your home | Apt. no.

City, town or post office, state, and ZIP code. If you have a foreign address, also complete the spaces below. See instructions. | If this is an amended return, check here ▶ ☐

Foreign country name | Foreign province/state/county | Foreign postal code

If you **only** owe the additional 10% tax on early distributions, you may be able to report this tax directly on Schedule 2 (Form 1040 or 1040-SR), line 6, or Form 1040-NR, line 57, without filing Form 5329. See the instructions for Schedule 2 (Form 1040 or 1040-SR), line 6, or for Form 1040-NR, line 57.

Part I **Additional Tax on Early Distributions.** Complete this part if you took a taxable distribution (other than a qualified disaster distribution) before you reached age 59½ from a qualified retirement plan (including an IRA) or modified endowment contract (unless you are reporting this tax directly on Form 1040, 1040-SR, or 1040-NR—see above). You also may have to complete this part to indicate that you qualify for an exception to the additional tax on early distributions or for certain Roth IRA distributions. See instructions.

1	Early distributions included in income. For Roth IRA distributions, see instructions	1	
2	Early distributions included on line 1 that are not subject to the additional tax (see instructions). Enter the appropriate exception number from the instructions: ______	2	
3	Amount subject to additional tax. Subtract line 2 from line 1	3	
4	**Additional tax.** Enter 10% (0.10) of line 3. Include this amount on Schedule 2 (Form 1040 or 1040-SR), line 6, or Form 1040-NR, line 57	4	
	Caution: If any part of the amount on line 3 was a distribution from a SIMPLE IRA, you may have to include 25% of that amount on line 4 instead of 10%. See instructions.		

Part II **Additional Tax on Certain Distributions From Education Accounts and ABLE Accounts.** Complete this part if you included an amount in income, on Schedule 1 (Form 1040 or 1040-SR), line 8, or Form 1040-NR, line 21, from a Coverdell education savings account (ESA), a qualified tuition program (QTP), or an ABLE account.

5	Distributions included in income from a Coverdell ESA, a QTP, or an ABLE account	5	
6	Distributions included on line 5 that are not subject to the additional tax (see instructions)	6	
7	Amount subject to additional tax. Subtract line 6 from line 5	7	
8	**Additional tax.** Enter 10% (0.10) of line 7. Include this amount on Schedule 2 (Form 1040 or 1040-SR), line 6, or Form 1040-NR, line 57	8	

Part III **Additional Tax on Excess Contributions to Traditional IRAs.** Complete this part if you contributed more to your traditional IRAs for 2019 than is allowable or you had an amount on line 17 of your 2018 Form 5329.

9	Enter your excess contributions from line 16 of your 2018 Form 5329. See instructions. If zero, go to line 15			9	
10	If your traditional IRA contributions for 2019 are less than your maximum allowable contribution, see instructions. Otherwise, enter -0-	10			
11	2019 traditional IRA distributions included in income (see instructions)	11			
12	2019 distributions of prior year excess contributions (see instructions)	12			
13	Add lines 10, 11, and 12			13	
14	Prior year excess contributions. Subtract line 13 from line 9. If zero or less, enter -0-			14	
15	Excess contributions for 2019 (see instructions)			15	
16	Total excess contributions. Add lines 14 and 15			16	
17	**Additional tax.** Enter 6% (0.06) of the **smaller** of line 16 **or** the value of your traditional IRAs on December 31, 2019 (including 2019 contributions made in 2020). Include this amount on Schedule 2 (Form 1040 or 1040-SR), line 6, or Form 1040-NR, line 57			17	

Part IV **Additional Tax on Excess Contributions to Roth IRAs.** Complete this part if you contributed more to your Roth IRAs for 2019 than is allowable or you had an amount on line 25 of your 2018 Form 5329.

18	Enter your excess contributions from line 24 of your 2018 Form 5329. See instructions. If zero, go to line 23			18	
19	If your Roth IRA contributions for 2019 are less than your maximum allowable contribution, see instructions. Otherwise, enter -0-	19			
20	2019 distributions from your Roth IRAs (see instructions)	20			
21	Add lines 19 and 20			21	
22	Prior year excess contributions. Subtract line 21 from line 18. If zero or less, enter -0-			22	
23	Excess contributions for 2019 (see instructions)			23	
24	Total excess contributions. Add lines 22 and 23			24	
25	**Additional tax.** Enter 6% (0.06) of the **smaller** of line 24 **or** the value of your Roth IRAs on December 31, 2019 (including 2019 contributions made in 2020). Include this amount on Schedule 2 (Form 1040 or 1040-SR), line 6, or Form 1040-NR, line 57			25	

For Privacy Act and Paperwork Reduction Act Notice, see your tax return instructions. Cat. No. 13329Q Form **5329** (2019)

Form 5329 (2019) Page 2

Part V **Additional Tax on Excess Contributions to Coverdell ESAs.** Complete this part if the contributions to your Coverdell ESAs for 2019 were more than is allowable or you had an amount on line 33 of your 2018 Form 5329.

26	Enter the excess contributions from line 32 of your 2018 Form 5329. See instructions. If zero, go to line 31			26	
27	If the contributions to your Coverdell ESAs for 2019 were less than the maximum allowable contribution, see instructions. Otherwise, enter -0-	27			
28	2019 distributions from your Coverdell ESAs (see instructions)	28			
29	Add lines 27 and 28			29	
30	Prior year excess contributions. Subtract line 29 from line 26. If zero or less, enter -0-			30	
31	Excess contributions for 2019 (see instructions)			31	
32	Total excess contributions. Add lines 30 and 31			32	
33	**Additional tax.** Enter 6% (0.06) of the **smaller** of line 32 **or** the value of your Coverdell ESAs on December 31, 2019 (including 2019 contributions made in 2020). Include this amount on Schedule 2 (Form 1040 or 1040-SR), line 6, or Form 1040-NR, line 57			33	

Part VI **Additional Tax on Excess Contributions to Archer MSAs.** Complete this part if you or your employer contributed more to your Archer MSAs for 2019 than is allowable or you had an amount on line 41 of your 2018 Form 5329.

34	Enter the excess contributions from line 40 of your 2018 Form 5329. See instructions. If zero, go to line 39			34	
35	If the contributions to your Archer MSAs for 2019 are less than the maximum allowable contribution, see instructions. Otherwise, enter -0-	35			
36	2019 distributions from your Archer MSAs from Form 8853, line 8	36			
37	Add lines 35 and 36			37	
38	Prior year excess contributions. Subtract line 37 from line 34. If zero or less, enter -0-			38	
39	Excess contributions for 2019 (see instructions)			39	
40	Total excess contributions. Add lines 38 and 39			40	
41	**Additional tax.** Enter 6% (0.06) of the **smaller** of line 40 **or** the value of your Archer MSAs on December 31, 2019 (including 2019 contributions made in 2020). Include this amount on Schedule 2 (Form 1040 or 1040-SR), line 6, or Form 1040-NR, line 57			41	

Part VII **Additional Tax on Excess Contributions to Health Savings Accounts (HSAs).** Complete this part if you, someone on your behalf, or your employer contributed more to your HSAs for 2019 than is allowable or you had an amount on line 49 of your 2018 Form 5329.

42	Enter the excess contributions from line 48 of your 2018 Form 5329. If zero, go to line 47			42	
43	If the contributions to your HSAs for 2019 are less than the maximum allowable contribution, see instructions. Otherwise, enter -0-	43			
44	2019 distributions from your HSAs from Form 8889, line 16	44			
45	Add lines 43 and 44			45	
46	Prior year excess contributions. Subtract line 45 from line 42. If zero or less, enter -0-			46	
47	Excess contributions for 2019 (see instructions)			47	
48	Total excess contributions. Add lines 46 and 47			48	
49	**Additional tax.** Enter 6% (0.06) of the **smaller** of line 48 **or** the value of your HSAs on December 31, 2019 (including 2019 contributions made in 2020). Include this amount on Schedule 2 (Form 1040 or 1040-SR), line 6, or Form 1040-NR, line 57			49	

Part VIII **Additional Tax on Excess Contributions to an ABLE Account.** Complete this part if contributions to your ABLE account for 2019 were more than is allowable.

50	Excess contributions for 2019 (see instructions)	50	
51	**Additional tax.** Enter 6% (0.06) of the **smaller** of line 50 **or** the value of your ABLE account on December 31, 2019. Include this amount on Schedule 2 (Form 1040 or 1040-SR), line 6, or Form 1040-NR, line 57	51	

Part IX **Additional Tax on Excess Accumulation in Qualified Retirement Plans (Including IRAs).** Complete this part if you did not receive the minimum required distribution from your qualified retirement plan.

52	Minimum required distribution for 2019 (see instructions)	52	
53	Amount actually distributed to you in 2019	53	
54	Subtract line 53 from line 52. If zero or less, enter -0-	54	
55	**Additional tax.** Enter 50% (0.50) of line 54. Include this amount on Schedule 2 (Form 1040 or 1040-SR), line 6, or Form 1040-NR, line 57	55	

Sign Here Only if You Are Filing This Form by Itself and Not With Your Tax Return

Under penalties of perjury, I declare that I have examined this form, including accompanying attachments, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

▶ Your signature ▶ Date

Paid Preparer Use Only	Print/Type preparer's name	Preparer's signature	Date	Check ☐ if self-employed	PTIN
	Firm's name ▶			Firm's EIN ▶	
	Firm's address ▶			Phone no.	

Form **5329** (2019)

APPENDIX E– QLAC MATERIALS

A PRACTICAL APPROACH TO QUALIFYING LONGEVITY ANNUITY CONTRACTS (QLACS)

Using the (King) L.E.A.R. (Life Expectancy and Return) analysis to determine whether clients should invest in specially designed annuity products under their IRA or Qualified Retirement Plans.

"Who loses and who wins; who's in, who's out.

And take upon the mystery of things . . ."

[LISI Employee Benefits & Retirement Planning Newsletter #639 (August 20, 2014) at http://www.leimbergservices.com]

BY ALAN S. GASSMAN, ESQUIRE, CHRISTOPHER J. DENICOLO, ESQUIRE, AND BRANDON KETRON

EXECUTIVE SUMMARY

The insurance industry received a July 4th gift from the Internal Revenue Service in the form of a Final Regulations released on July 1, 2014 which make it possible to place a portion of IRA/Plan investments into fixed annuities called "Qualified Longevity Annuity Contracts" (QLACs) that will enable the IRA holder or plan participant to avoid the Required Minimum Distribution rules that apply after age 70½ to the extent that IRA or plan assets are held under such vehicles. The maximum amount that can be contributed into such fixed annuities under an IRA/Plan will be the lesser of $125,000 or 25% of the value of the IRA/Plan account as of the time of the investment. The $125,000 limitation applies cumulatively to all IRA/Plan accounts that the taxpayer has, and the 25% limitation applies cumulatively to the account balance of all of such IRA/Plan accounts.

Essentially, the value of such contracts will not be considered to be assets of the IRA/Plan for purposes of the Required Minimum Distribution rules until the owner is age 85. The authors have developed the L.E.A.R. (Life Expectancy and Return) analysis spreadsheets to enable planners to determine if and when QLACs will be worthwhile for their clients. The main factor is the expected life expectancy of the account holder and their Surviving Spouse.

The basic QLAC requirements are that the annuity contract must state that it will pay fixed dollar amounts at stated intervals over a number of years for the life of a taxpayer, beginning no later than when the taxpayer reaches the age of 85. These payments distributed from the QLAC are fully taxable and will not count towards the individual's Required Minimum Distribution obligations relating to non-QLAC retirement plan assets.

If the taxpayer dies before he or she has received payments equal to the amount paid for the contract, the contract may offer a return of premium option, but this option is not required by the Regulations. The return of premium amount can be paid to the beneficiary's IRA/P la n account, but no more than the premium amount can be paid under this option. Thus, if the taxpayer dies before he or she has received more than his or her investment back there is, at best, a zero rate of return.

On the other hand, if the taxpayer or his or her Designated Beneficiaries have a life payment contract, and outlive their applicable life expectancy, then the rate of return on the contract can be positive, and they can be assured of "never running out of money." However, inflation and taxes may cause the real value of the payments to be lower than one might expect. Wealthy clients with long life expectancies may therefore be well suited to purchase $125,000 in QLACs for their IRA/Plan.

FACTS

The applicable Final QLAC Treasury Regulations Sections 1.401(a)(9)-5, Q & A-3, .401(a) (9)-6, Q & A-12, 1.401(a)(9)-6 Q & A-17, 1.403(b)-6(e)(9) and 1.408-8, Q & A-12 allow QLACs to be held under non-Roth IRAs, defined contribution plans, and Section 403(b), and 457(b) plans, but not under defined benefit plans or Roth IRAs.[151] These Final Regulations replace Proposed Regulations that were issued in 2012 to allow commentary on this concept. The Final Regulations are substantially similar to the 2012 Proposed Regulations, with minor changes that are noteworthy as to policy and application.

According to the Final Regulations, QLACs may not be variable or equity indexed annuities, even if they offer a guaranteed minimum rate of return, unless or until explicitly approved by the Internal Revenue Service. Instead, QLACs must be annuity contracts with a fixed rate of return, life payment, or other similar features. The preamble to the new Regulations points out that variable and equity indexed annuities with contractual guarantees provide an unpredictable level of income to the holder and are therefore inconsistent with the purpose of the new Regulations. It is interesting that hybrid index annuity sales literature often touts protection of principal and reliable rates of return. The drafters of the new Regulations seem to disagree with these assertions.

QLAC Math – Donald Duck in Mathematics Land?

The premiums paid for a QLAC cannot exceed the lesser of $125,000 or 25% of the IRA/Plan account balance as of the last valuation date preceding the date of a premium payment. This is increased for post-valuation date contributions added to the account and decreased for post-valuation date distributions made from the account. The QLAC's value is excluded from the account balance that is used to calculate the annual Required Minimum Distributions. However,

[151] For the purposes of this article, all references to "IRAs" refer only to non-Roth IRAs, including traditional IRAs described in Internal Revenue Code Section 408, SEP IRAs and SIMPLE IRAs, but not Roth IRAs unless specifically provided.

the value of the QLAC is included for applying the 25% limit. The IRS kept the dollar and percentage limit to "constrain undue deferral of distribution of an employee's interest."[152]

Next Calendar Year Correction Right - The Proposed Regulations stated that if the above premium limits were exceeded, then the contract would fail to be a QLAC. Fortunately, the Final Regulations provide that the contract will not fail to be a QLAC if any such excess portion is returned to the taxpayer's non-QLAC portion of his or her IRA/Plan by the end of the calendar year following the calendar year in which the excess premium was paid. This excess can be returned to the account in cash or in the form of an annuity contract that is not intended to be a QLAC. If at any time the QLAC or intended QLAC contract fails for reasons other than exceeding premium limits, the contract will not be treated as a QLAC from the date of the first premium payment. Any increase must exceed \$10,000 to apply for a given year. The 2012 Proposed Regulations had provided for a \$25,000 multiple to apply.

Inflation Adjustments to \$125,000 Amount in \$10,000 Increments – The \$125,000 dollar amount limitation described above will be adjusted for inflation in the same time and manner as under section 415(d) except: (1) The base period will be the quarter beginning six months before the effective date of the Regulation (the effective date of the Regulations is July 2, 2014, so the quarter beginning six months before the effective date appears to be January 1, 2014); and (2) any increase must exceed\$10,000 to apply for a given year. The 2012 Proposed Regulations had provided for a \$25,000 multiple to apply.

QLAC Payment Deferral Can Only Last Until Age 85, Or Possibly Later If Mortality Tables Change - The annuity contract must provide for distributions to be made no later than a specific annuity starting date. This date cannot be later than the first day of the month following the taxpayer attaining age of 85. A taxpayer can elect to have an earlier annuity starting date, but the contract is not required to have an option to start distributions before the annuity starting date. The maximum age may be adjusted based on changes in mortality, although in Bulletin 2014-30, the IRS stated that it believes that these changes will not occur more often than the dollar limit adjustment.

Must be a Fixed Annuity - A variable contract under Internal Revenue Code Section 817, an indexed contract or, a similar contract will not qualify as a QLAC but the Commissioner may create an exception to this rule. However, a participating annuity contract is not similar to a variable contract or indexed contract just because it has payments of dividends as described in Treasury Regulation Section 1.401(a)(9)-6, A-14(c)(3). The Regulation also noted that a contract that has a cost- of- living adjustment discussed in Treasury Regulation Section 1.401(a)(9)-6, A-14(b), is not considered similar to a variable or indexed contract.

Illiquidity Required - A QLAC cannot make available any commutation benefit, cash surrender value, or other similar feature. In other words, the money invested in the QLAC is illiquid and irrevocable, which is an important factor to consider before a taxpayer invests in a QLAC.

[152] Internal Revenue Bulletin 2014-30, TD 9673.

According to Bulletin 2014-30, this prohibition is in place because this "feature would significantly reduce the benefit of mortality pooling under the contracts."[153]

Death Benefits of a QLAC

A QLAC may offer a return of premium after the death of the account holder that can be paid before or after the annuity starting date to the extent that the contract has not provided a return of the aggregate premium amount paid for the QLAC.[154] The return of premium can be in place of a life annuity provided to a Surviving Spouse or Designated Beneficiary. A return of premium payment must be paid in a single lump sum to the beneficiary of the QLAC before the end of the year following the year of the account holder's or Surviving Spouse's death, as applicable. If the applicable death occurs on or before the required annuitization date for the account holder or his or her Surviving Spouse (no later than age 85), then the return of premium is considered as the balance of the IRA/Plan account value that can be rolled over by the Surviving Spouse into his or her own IRA, or can be transferred into an inherited IRA for the benefit of the non-spouse beneficiary. However, if the applicable death occurs after the required annuitization date then the return of premium is seen as a Required Minimum Distribution for the year in which it is paid. The return of premium must be paid out to the account beneficiary when received from the carrier and is fully taxable and cannot be rolled over into another Qualified Retirement Plan.

If the only beneficiary of the QLAC is the account holder's Surviving Spouse, and the account holder's death occurs on or after the annuity start date, then the only benefit allowed to be paid (other than a return of premium) is a life annuity that cannot exceed 100% of the annuity payment payable to the account holder.[155] There is a special exception that allows a QLAC to provide a qualified pre-retirement survivor annuity defined in Internal Revenue Code Section 417(c)(2) in order to compensate the Surviving Spouse for the loss of retirement benefits that would have otherwise been paid to the deceased employee.

If there are multiple beneficiaries where one of which is the Surviving Spouse, then the QLAC can be treated as if there were a separate QLAC for each beneficiary so that the special rules applicable only to the Surviving Spouse would apply. This is only allowed if certain rules are satisfied.[156] If the account holder's death occurs before the annuity starting date, the only benefit payable (other than a return of premium as described above) is a life annuity where the periodic annuity payment is not more than 100% of the annuity payment that would have been available to the account

[153] Internal Revenue Bulletin 2014-30.

[154] Treas. Reg. § 1.401(a)(9)-6, A-17(c)(4)- Return of premiums—(i) In general. In lieu of a life annuity payable to a Designated Beneficiary under paragraph (c)(1) or (2) of this A-17, a QLAC is permitted to provide for a benefit paid to a beneficiary after the death of the employee in an amount equal to the excess of— (a) The premium payments made with respect to the QLAC over The payments already made under the QLAC.

[155] Treas. Reg. § 1.401(a)(9)-6, A-17(c)(1)(i): If the employee dies on or after the annuity starting date for the contract and the employee's Surviving Spouse is the sole beneficiary under the contract then, except as provided in paragraph (c)(4) of this A-17, the only benefit permitted to be paid after the employee's death is a life annuity payable to the Surviving Spouse where the periodic annuity payment is not in excess of 100 percent of the periodic annuity payment that is payable to the employee.

[156] Treas. Reg. § 1.401(a)(9)-8, A-2(a) and A-3.

holder.[157] However, it may exceed 100% if necessary to satisfy the requirements for a qualified preretirement survivor annuity.

If the Surviving Spouse is not the only beneficiary, and the account holder's death occurs on or after the annuity starting date, then the only benefit to be paid (other than a return of premium) is a life annuity payable to a beneficiary.[158] The life annuity is not allowed to exceed an applicable percentage of the annuity payment payable to the employee under Treasury Regulation Section 1.401(a)(9)-6, A-17(c)(2)(iii).[159] The percentage is provided in one of the two tables listed in the Section. Determining which table applies depends on the different types of death benefits that can be paid to the beneficiary under the contract. The first table described in A-2(c) of Treasury Regulation Section 1.401(a)(9)-6[160] provides the applicable percentage distribution that must be made to the non-spouse beneficiary after the account holder's death, and this table may only be used if the contract provides that if the account holder dies before the annuity start date, then no death benefits are payable to a non-spouse beneficiary. However, if the account holder dies on or after his or her annuity start date, then the non-spouse beneficiary can receive a life annuity based on the above- referenced table. Additionally, this table is available only if no benefits are payable under the contract where the taxpayer selects an earlier annuity starting date than the specified starting date under the contract and dies less than 90 days after making that election. This second part of the requirement is to avoid taxpayers with shortened life expectancies from circumventing the first part of the rule.

[157] Treas. Reg. § 1.401(a)(9)-6, A-17(c)(1)(ii)(A): Amount of annuity. If the employee dies before the annuity starting date and the employee's Surviving Spouse is the sole beneficiary under the contract then, except as provided in paragraph (c)(4) of this A-17, the only benefit permitted to be paid after the employee's death is a life annuity payable to the Surviving Spouse where the periodic annuity payment is not in excess of 100 percent of the periodic annuity payment that would have been payable to the employee as of the date that benefits to the Surviving Spouse commence. However, the annuity is permitted to exceed 100 percent of the periodic annuity payment that would have been payable to the employee to the extent necessary to satisfy the requirement to provide a qualified preretirement survivor annuity (as defined under section 417(c)(2) or ERISA section 205(e)(2)) pursuant to section 401(a)(11)(A)(ii) or ERISA section 205(a)(2).(B) Commencement date for annuity. Any life annuity payable to the Surviving Spouse under paragraph (c)(1)(ii)(A) of this A-17 must commence no later than the date on which the annuity payable to the employee would have commenced under the contract if the employee had not died

[158] Treas. Reg. § 1.401(a)(9)-6, A-17(c)(2)(i): If the employee dies on or after the annuity starting date for the contract and the employee's Surviving Spouse is not the sole beneficiary under the contract then, except as provided in paragraph (c)(4) of this A-17, the only benefit permitted to be paid after the employee's death is a life annuity payable to the Designated Beneficiary where the periodic annuity payment is not in excess of the applicable percentage (determined under paragraph (c)(2)(iii) of this A-17) of the periodic annuity payment that is payable to the employee.

[159] (iii) Applicable percentage—(A) Contracts without pre-annuity starting date death benefits. If, as described in paragraph (c)(2)(iv) of this A-17, the contract does not provide for a pre-annuity starting date non-spousal death benefit, the applicable percentage is the percentage described in the table in A-2(c) of this section.

[160] The table can be found here: http://www.law.cornell.edu/cfr/text/26/1.401%28a%29%289%29-6.

The second table is described in Treasury Regulation Section 1.401(a)(9)-6, A-17(c)(2)(iii)(D).[161]

This table is used where the contract provides a pre-annuity start date death benefit to a non- spouse beneficiary. Under the 2012 Proposed QLAC Regulations, the use of this table was limited to contracts that only allowed non-spouse beneficiaries to be irrevocably selected as of the annuity start date. However, the Final QLAC Regulations changed this rule to allow non-spouse beneficiaries to be selected at a different time in certain situations. It is important to note that there is no violation of this irrevocability requirement when an account holder substitutes his or her spouse as the beneficiary. If the account holder's spouse is not the only beneficiary, and the account holder's death occurs before the annuity starting date, then the only payment available (other than a return of premium) is a life annuity where the payment is not more than the applicable percentage, under 1.401(a)(9)-6, A-17(c)(2)(iii), of the amount that would have been payable to the account holder.

Other QLAC Requirements

When the QLAC is issued, the taxpayer must be notified that it is intended to be a QLAC. This is to make sure the issuer, taxpayer, plan sponsor, and IRS all know that the QLAC rules apply to this contract. This requirement is satisfied if this language is in the contract, or in a rider or

[161] Adjusted employee/beneficiary age difference Applicable percentage:

2 years or less	100%
3	88%
4	78%
5	70%
6	63%
7	57%
8	52%
9	48%
10	44%
11	41%
12	38%
13	36%
14	34%
15	32%
16	30%
17	28%
18	27%
19	26%
20	25%
21	24%
22	23%
23	22%
24	21%
25 and greater	20%

endorsement to the contract. It can also be satisfied if a certificate is issued under a group annuity contract, and the certificate states that the taxpayer's interest is to be a QLAC.

In order to avoid surrender charges on current contracts that do not qualify as QLACs because of inadequate notice, there is a transition rule where any annuity contract dated before January 1, 2016 will not fail due to the notification requirement as long as the taxpayer is notified that the contract is intended to be a QLAC and is amended (or a rider, amendment to the certificate, or endorsement to the contract is issued) no later than December 31, 2016 to indicate that the contract is intended to be a QLAC.

Distributions must satisfy the requirements of Internal Revenue Code Section 401(a)(9) dealing with annuities in Treasury Regulation Section 1.401(a)(9)-6, except for the requirement that annuity payments commence on or before the taxpayer's beginning date.

Section 403(b) Plans and Section 457(b) Plans

The Final Regulations apply the QLAC qualified plan rules when a QLAC is purchased under an eligible Section 403(b) or Section 457(b) plan, rather than the rules applicable to IRAs, which are described below.

IRAs

The QLAC rules that apply to IRAs are significantly similar to the QLAC rules that apply to defined contribution retirement plans and Section 403(b) or 457(b) plans, as described above, with a few minor differences.

As applicable to defined contribution retirement plans and Section 403(b) or 457(b) plans, the amount of premiums paid for the contract under an IRA cannot exceed the lesser of 25% of the IRA account balance or $125,000 in order to be a QLAC. This limit is reduced by the amount of premium payments made for the same contract or any other contract that was meant to be a QLAC under the IRA or any IRA, plan, or annuity.

However, the Final Regulations allow a QLAC that may be bought under an IRA within these premium limits to be purchased under another, separate IRA. Thus, the amount of the premium paid cannot be more than the lesser of 25% of the aggregate account balance of all of such accounts or $125,000. This limit is reduced by the amount of premium payments made for the same contract or any other contract that was meant to be a QLAC under the IRA or any IRA, plan, or annuity. The Regulations also state that the trustee, custodian, or issuer of the IRA may rely on the IRA owner's information on the amount of premiums for the dollar and percentage limits, and the amount of the IRA account balances for the purposes of the percentage limits, unless the trustee, custodian, or issuer of the IRA has knowledge to the contrary.

Since Roth IRAs are only subject to the minimum distribution rules after the death of the owner, an annuity bought under a Roth IRA is not treated as a QLAC. If a QLAC was purchased under a non-Roth IRA and that IRA is later converted or rolled over to a Roth IRA, then the QLAC would cease being a QLAC at the time of the conversion.

IRA QLACs Better for Men, Non-IRA QLACs Better for Women

One important consideration is that QLACs purchased under an IRA must use gender-distinct life expectancy tables to determine the premium or monthly payout, and QLACs purchased under a non-IRA retirement plan must use gender-neutral life expectancy tables. This means that if a male taxpayer was faced with the alternative of purchasing the same QLAC under an IRA or under a non- IRA retirement plan, the IRA would result in a higher payout due to a shorter life expectancy being applicable to males versus the life expectancy that would apply under the gender-neutral tables. In comparison, if a female taxpayer purchased the same QLAC under an IRA or a non-IRA retirement plan, then the non-IRA retirement plan would result in a higher payout because the female-specific life expectancy tables reflect a longer life expectancy than the gender-neutral tables. For example, a 72-year-old woman might have a 17.32-year life expectancy under the IRA gender-distinct tables, and a 15.59-year life expectancy (as does a man) under the gender-neutral tables that are applicable to non-IRA retirement plans. A 72-year-old man might have a 14.26-year life expectancy under then IRA ender-distinct tables.

Defined Benefit Plans

The QLAC Regulations do not allow for the changed minimum payout rules to apply for defined benefit pension plans. Many defined benefit plans can be converted into rollover IRAs and can then purchase QLAC contracts.

Initial Disclosure and Annual Reporting Requirements

The Final Regulations do not call for an initial disclosure requirement specifically applicable to QLACs because of the disclosure practices that are in place for Qualified Retirement Plans under state law and Title I of ERISA. The Proposed Regulations had disclosure requirements that are fortunately not required by the Final Regulations.

There are pension plan annual reporting requirements under Internal Revenue Code Section 6047(d) that require annual reports to be filed with the IRS and a statement be given to the employee with the status of the contract. The report must contain, at a minimum, the following:

- The name, address, and identifying number of the issuer of the contract, along with information on how to contact the issuer for more information about the contract;
- The name, address, and identifying number of the individual in whose name the con- tract has been purchased;
- If the contract was purchased under a plan, the name of the plan, the plan number, and the Employer Identification Number (EIN) of the plan sponsor;
- If payments have not yet commenced, the annuity starting date on which the annuity is scheduled to commence, the amount of the periodic annuity payable on that date, and whether that date may be accelerated;

- For the calendar year, the amount of each premium paid for the contract and the date of the premium payment;
- The total amount of all premiums paid for the contract through the end of the calendar year; and
- The fair market value of the QLAC as of the close of the calendar year.

The issuer of the QLAC is also required to furnish to the taxpayer a statement with this information on or before January 31 following the year the report is required. These reports must be given each year starting with the year premiums are paid and ending when the taxpayer reaches the age of 85 or dies. If the sole beneficiary of the QLAC is the spouse and the taxpayer dies, the reporting requirement continues until the earlier of the year when distributions to the Surviving Spouse begin or the year in which the Surviving Spouse dies.

Effective/Applicability Dates

These Regulations became effective July 2, 2014. If an existing contract is traded for a contract that meets the QLAC requirements on or after this date, then the new contract may qualify as a QLAC and will be treated as obtained on the date of the exchange. In this situation, the fair market value of the original contract will act as the premium that counts towards the QLAC premium limit.

COMMENT

QLACs offer taxpayers the opportunity to defer income taxes that would otherwise result from the larger Required Minimum Distributions that would apply if a portion of the taxpayer's IRA or other retirement plan were not used to purchase a QLAC. However, the widespread prevalence of QLACs in the marketplace might not occur for some time, as the authors are not aware of any life insurance or annuity companies having released their QLAC products as of the time of this writing. In any event, the choice of investing in a QLAC turns on several factors, the most significant of which are whether the taxpayer wants fixed income features in the portfolio and whether the taxpayer will live long enough to realize a positive rate of return. Therefore, it is important to run an appropriate analysis, such as the L.E.A.R. analysis, to consider the taxpayer's life expectancy and possible rates of return on the investment in the QLAC.

Under a typical QLAC arrangement, a taxpayer could invest $125,000 (the maximum amount that can be invested is the lesser of (1) 25% of the value of the qualified account at the time of the investment; or (2) $125,000) into a deferred income annuity contract that would pay-out monthly income at an elected age (not to exceed 85) to the taxpayer.

One very knowledgeable advisor, Michael Morrissey of Vanguard's annuity division gave the authors the following example of how a hypothetical QLAC might perform:

A 65-year-old male who wants to receive a monthly income of $1,000 per month for life beginning at age 80 can pay $47,920 for a life annuity right now. The annuity contract would include not only the above payments, but also a refund on death to the extent that the total payments received before death did not amount to $47,920. The value of this contract would not be subject to the Required Minimum Distribution rules until the gentleman reaches age 80.

The new Regulations require that payments from a QLAC must begin to be made by age 85. A 65 year-old male who wants to receive $1,000 a month for life beginning at age 85 would only have to pay $26,634 for a Vanguard life annuity contract, which would also provide a refund to the extent that total payments are less than $26,634 upon death.

In both of the above arrangements there is a death benefit feature, which provides that if the account holder dies before receiving payments equal to the amount invested, then the deficit amount will be paid to the account holder's beneficiaries (typically without interest) shortly after his or her death. In the alternative, payments might continue for the lifetime of a Surviving Spouse who could roll the annuity over to his or her own IRA and continue to have the benefit of payment rights. If the account holder dies before the elected age to begin distributions, the new Regulations allow a contract to return only the principal amount invested.

The death benefit restrictions are a major drawback of the new Regulations. These restrictions essentially require an account holder to outlive his or her life expectancy in order to receive a positive rate of return.

In the above-mentioned example, a 65-year-old male who contributes $47,920 to receive monthly income of $1,000 at the age of 80 would have to live for 48 months (age 84) in order to receive a positive rate of return. If the gentleman passed away before this time period, then he would receive only a return of principal, meaning that his rate of return would be zero. Based on IRS published life expectancy Table 2000CM, the average 65-year-old male has a 46% chance to live long enough to receive a positive rate of return. In order to receive a rate of return of roughly 3%, the gentleman would have to live until age 86. Under Table 2000CM, the gentleman has a 37% chance of living until age 86.

The authors have prepared a spreadsheet to illustrate the financial utility and tax implications of acquiring a QLAC under an IRA, relative to retaining in the IRA and continuing to invest in accordance with past practices the funds otherwise used to acquire the QLAC. One example assumes that a 65-year-old male taxpayer has $500,000 in an IRA that is growing at 3.5% per year. The taxpayer invests the maximum premium amount of $125,000 into a QLAC that will provide yearly payments of $51,948 beginning when the taxpayer reaches age 85. When Required Minimum Distributions from the IRA begin upon the taxpayer attaining the Required Beginning Date, the QLAC will not count as part of the IRA balance, resulting in a reduction of the minimum distribution for that year by $5,697.02 and resulting tax savings (deferral) for that year of $2,220.73. At the age of 85 when the QLAC will begin to make payments, the taxpayer will have total tax savings of $40,916.31.

All payments from the QLAC are fully taxable and made directly to the taxpayer, not into the IRA or other applicable retirement plan. The taxpayer is still required to take the Required Minimum Distributions from the non-QLAC portion of his or her IRA or other applicable retirement plan, because neither the value of the QLAC nor the payments therefrom will count in determining the minimum distribution requirements. Any payments from the QLAC that occur after the annuitization beginning date will satisfy the Required Minimum Distributions relating to the value of the QLAC.

From an investment standpoint, the benefit of investing in a QLAC backfires and causes more harm than good if the taxpayer does not live long enough to have the contract provide a positive rate of return. For example, assume that the taxpayer does not invest $125,000 in the QLAC, and instead leaves the funds in the IRA growing at 3.5% per year in order to compare the two options. For the investment in the QLAC to provide a greater rate of return, than 3.5%, the individual would have to live to the age of 90. If the IRA was to grow at 6% per year, then the individual would have to live to the age of 95 in order for the QLAC to provide a higher rate of return. The longer that the individual lives, the greater the rate of return will be. Below is a chart comparing the two options at a 3.5% rate of return and at a 6% rate of return, based upon the value of the applicable portion of the IRA. A detailed spreadsheet showing the results of these options is available upon request.

CONCLUSION

The QLAC Regulations provide a flexible and possibly advantageous (but complicated) planning opportunity that could boost the popularity of longevity annuities as a retirement planning tool. The applicable Regulations provide potential tax savings by allowing a taxpayer to delay a portion of Required Minimum Distributions from a retirement plan until the taxpayer reaches the age of 85, although the potential tax savings could be offset by the financial performance of the QLAC relative to other investments if the taxpayer does not live to a certain age.

There will be doubtlessly be interaction and confusion between these rules and the QLAC products, and between the traditional IRA/Plan investments typically undertaken by taxpayers and/or their plan administrators and QLACs from a financial investment standpoint. Practitioners would greatly benefit from literature and illustrations showing the real financial impact and results (taking into account both tax savings AND financial performance) of investing in a QLAC, which hopefully will be made available to the public when (or soon after) carriers release QLAC into the marketplace. It is important that planners run appropriate analysis to determine whether a QLAC is a right fit for the client, in light of the client's possible life expectancy and expected rates of return from the investment.

APPENDIX F

LISI EMPLOYEE BENEFITS & RETIREMENT PLANNING NEWSLETTER #668 (FEBRUARY 7, 2017) AT HTTP://WWW.LEIMBERGSERVICES.COM

BY BRANDON KETRON AND ALAN GASSMAN

Can I use My IRA to Start a Business?
Maybe, But with Great Power,
Comes Great Responsibility

One potential way for an entrepreneur to fund a new business is with his or her retirement plan assets. This is known as a Rollover as Business Start Up Plan (ROBS).

A typical ROBS plan involves forming a new C-Corporation and adopting a simple 401(k) plan. The entrepreneur can then roll over his or her IRA account into the new 401(k) plan. The 401(k) plan then purchases stock in the new corporation. This results in the funding of a new corporation with the entrepreneur's former IRA account.

The benefits of this strategy include:

1. The ability to fund a business with Retirement Assets while avoiding taxes on withdrawal and the 10% penalty on early withdrawals.

2. An alternate to traditional debt-based financing.

3. Gains from the sale of stock in the business will be deferred until the assets are withdrawn from the Retirement Account.

4. A creditor protected vehicle that can be safeguarded notwithstanding judgments against a 401(k) account holder who may also receive wages for services rendered that may be creditor protected depending upon applicable state law.

But with great power, comes great responsibility. The IRS heavily scrutinizes these types of arrangements and has issued literature as to the technical reasons why they might be seen as problematic. The IRS has not issued any specific adverse rulings related to ROBS plans but does target ROBS plans for other violations of retirement account rules. Entrepreneurs should consult with the appropriate advisors in order to comply with the complex rules involved with a ROBS Plan. If a ROBS plan is undertaken it will be important to make sure that all i's are dotted and all t's are crossed due to the fact that one small mistake will result in a termination and taxable distribution of the entire retirement account.

Now, Brandon Ketron and Alan Gassman provide members with their commentary on the ROBS planning technique.

Here is their commentary:

EXECUTIVE SUMMARY

One potential way for an entrepreneur to fund a new business is with his or her retirement plan assets. This is known as a Rollover as Business Start Up Plan (ROBS).

A typical ROBS plan involves forming a new C-Corporation and adopting a simple 401(k) plan. The entrepreneur can then roll over his or her IRA account into the new 401(k) plan. The 401(k) plan then purchases stock in the new corporation. This results in the funding of a new corporation with the entrepreneur's former IRA account.[162]

While ROBS Plans do not violate the prohibited transaction rules per se, the IRS heavily scrutinizes these plans to ensure their compliance with these complex rules. If a Plan Participant engages in a prohibited transaction, the plan will be disqualified and result in a deemed taxable distribution of the entire account balance, which will also be subject to the 10% excise tax if the Plan Participant is under the age of 59½.

It is important to note that while a ROBS plan may satisfy the retirement plan rules initially, any failure to comply with the rules during the life of the plan will also result in a deemed distribution of the entire retirement plan.

COMMENT

The authors do not advocate or recommend that clients use their retirement plan or IRA assets to establish a ROBS, but it should be known that this is a possible way for entrepreneur clients to find capital to start a business. No-one should even think about starting a ROBS without specific written guidance from a qualified tax and ERISA lawyer. The C-corporation owned by the 401(k) plan will be taxed as a corporation and will be burdened by the compliance described herein, and possible future restrictive legislation. The following are some potential traps for the unwary involved with establishment and maintenance of a ROBS Plan.

1. Personal Guarantees of Corporate Loans

In *James E. Theissen et ux. v. Comm'r* and *Peek v. Comm'r* the Tax Court held that a personal guarantee of a corporate loan when the Plan Owner's IRA owned stock in the corporation was a prohibited transaction. As a result, the taxpayers' IRAs ceased to be IRAs as of the first day of the taxable year in which the guarantee occurred, and were deemed to have received distributions on that first day of the entire fair market value of their IRA assets.[163]

[162] *James E. Theissen et ux. v. Comm'r*, 146 T.C. 7 (2016); *Peek v. Comm'r*, 140 T.C. 216 (2013).

[163] For further discussion see LISI Employee Benefits & Retirement Planning Newsletter #654 (April 4, 2016) at http://www.leimbergservices.com, written by Steve Leimberg and Mike Jones.

These cases involved IRAs and not 401(k)s or ESOPs. It is unclear whether the same reasoning would apply to a ROBS Plan, but account owners and parties related thereto should strictly avoid personal guarantees of loans to be safe. Unrelated parties may be paid reasonable guarantee fees, but only from the business entity. Traditional lenders will be reluctant to lend to ROBS for concern of the tax impact of disqualification.

2. Payment of reasonable compensation to Entrepreneur. Unlike a self-directed IRA, a 401(k) or ESOP may pay compensation to the owner of the Plan and related parties, provided that the compensation is reasonable.

In *Ellis v. Commissioner*, the IRA owner purchased a used-car dealership inside of his IRA and ran the day-to-day operations of the business. The dealership paid the IRA owner reasonable compensation for his role as the manager of the business. The Tax Court held that the payment of compensation to the IRA owner was a prohibited transaction and resulted in the indirect use of plan assets for the benefit of the individual. Accordingly, the IRA was deemed distributed to the owner and the owner was immediately liable for taxes on the entire value plus the 10% excise tax and other applicable penalties and interest.[164]

Natalie Choate points out that this is particularly problematic for IRA-owned businesses. She states that "if your IRA-owned business cannot pay you compensation, you really cannot run a small business inside your IRA. If you work with no compensation, there is a risk of an 'assignment of income problem.'"[165]

Had Mr. Ellis rolled over his IRA into a 401(k) using a ROBS Plan, Mr. Ellis may have been able to avoid the prohibited transaction rules. The ERISA rules do not prevent an employee from taking a reasonable salary from a 401(k) owned business; however, the IRS may argue that the immediate payment of compensation to the Entrepreneur results in the indirect use of plan assets for the benefit of the individual. Entrepreneurs may consider only taking a salary from the profits of the company in order to avoid this characterization.

Additionally, any compensation paid to the Entrepreneur should be W-2 compensation, and not classified as 1099 independent contractor compensation.[166] In order for the Entrepreneur to participate in the 401(k) plan, he or she must be a legitimate employee of the Corporation. If the Entrepreneur fails to qualify as a qualified employee, the Plan may be disqualified.

[164] *Id.*

[165] See Choate, What Goes in Your IRA? None of Your Small Business! (September 11, 2015).

[166] Curry & Esposito, *You Invested 401(k) Money into Your Company: Common Myths and Important Compliance Reminders* (Presented January 24th, 2017, a copy of the slides can be obtained by emailing Jewell.Esposito@jacksonlewis.com).

3. Providing Direct or Indirect Services to an IRA

Leimberg and Jones caution that providing any kind of service to an IRA-owned business may constitute furnishing of services to the IRA by a disqualified person. This rule does not apply to a 401(k) or ESOP, and it is therefore vitally important to roll the funds over into an employer sponsored plan prior to providing any services to the company.

4. Lack of Notification of Plan Existence

If current or future employees are not notified of the existence of an ESOP or 401(k) plan, then it would cause a violation of the rule that a retirement plan must "be a definite, written program communicated to employees."[167]

If employees are not notified the Plan will be disqualified resulting in a taxable distribution of the entire Plan.

The IRS has cautioned against Entrepreneurs using independent contractors to avoid offering stock ownership to employees.[168] If an independent contractor is reclassified as an employee this could disqualify the entire Plan in addition to the other problems caused by this reclassification.

5. Plan Assets Used for Personal Expenses

A plan was disqualified when a corporation bought an RV for the business owner using some of the money it received in exchange for the stock of the corporation in a ROBS plan.[169] The use of corporate money or assets for personal expenses or purposes also presents other problems, so appropriate corporate formalities must be followed.

6. Stock Sale Must Be a Transaction for Adequate Consideration

ERISA exempts a plan's acquisition of employer stock from the prohibited transaction rules only if the purchase was for adequate consideration.[170] Therefore, a valuation of the business may need to be completed to have proof that the stock sale as part of the ROBS plan was for adequate consideration.[171]

7. Improper Use of Funds to Pay Promoter Fees

[167] LISI Employee Benefits & Retirement Planning Newsletter #471 (December 3, 2008) at http://www/leimbergservices.com, written by Natalie Choate.
[168] Michael D. Julianelle Guidelines Regarding Rollovers as Business Startups.
[169] *Id*.
[170] I.R.C. § 4975(d)(13).
[171] Michael D. Julianelle Guidelines Regarding Rollovers as Business Startups.

The IRS has stated that when a corporation uses part of the cash it raises from the stock sale to pay the fee of a promoter it may result in the indirect use of plan assets in a prohibited transaction.[172]

8. Discrimination in Favor of Highly Compensated Employees

Natalie Choate states that this is the IRS's best argument to disarm a ROBS, but that it is only useful against ROBS plans that have employees other than the plan owner and that do not in fact offer employer stock to rank and file employees.[173]

9. Failure to Issue a Form 1099-R when the Assets Are Rolled Over into the ROBS Plan.

A reputable CPA should be retained to assure that all proper tax returns and forms are filed, including the Form 1099-R.

10. Failure to file 5500's

A reputable actuary or qualified pension plan lawyer should be retained to assure that appropriate plan rules and formalities are followed, including the filing of a timely and accurately prepared Form 5500.

Conclusion

In conclusion, the IRS heavily scrutinizes these types of arrangements, and has issued literature as to the technical reasons why they might be seen as problematic. The IRS has not issued any specific adverse rulings related to ROBS plans but will target ROBS plans for other violations of retirement account rules. Entrepreneurs should consult with the appropriate advisors in order to comply with the complex rules involved with a ROBS Plan. If a ROBS plan is undertaken it will be important to make sure that all your I's are dotted and your T's crossed due to the fact that one mistake will result in a termination and taxable distribution of the entire retirement account.

172 *Id.*
173 *Id.*

APPENDIX G

SAMPLE RETIREMENT PLAN TRUST LANGUAGE AND TEA POT TRUST LANGUAGE

THE FOLLOWING LANGUAGE CAN BE USED IN TRUST AGREEMENTS TO WHICH IRA/PLANS ARE MADE PAYABLE IN ORDER TO HELP ASSURE QUALIFICATION OF THE TRUST AS A SEE-THROUGH TRUST.

IRA and Qualified Plan Beneficiary Provisions. In recognition that IRAs, qualified Retirement Plans, or similar benefits may be payable to this trust or one or more trusts herein established and that tax rules under Section 401(a)(9) of the Internal Revenue Code may be affected by the provisions herein applicable, the following shall apply to any such trust which is or becomes the direct or indirect beneficiary of a Retirement Plan that is not an Inherited IRA, notwithstanding any contrary provisions under this Agreement, except with respect to any marital deduction provision or marital deduction savings clause provision, or to the extent modified by the Qualified Plan/IRA Trust Protector under subsection (i) below:

(a) Definitions. For purposes of this Section:

(1) The term “minimum distribution rules” shall refer to the minimum required distribution rules promulgated under Section 401(a)(9) of the Internal Revenue Code as well as any similar rules promulgated by the Department of the Treasury.

(2) The term “Retirement Plan” or the term “Qualified Retirement Plan” shall refer to any plan or arrangement subject to the minimum distribution rules. The term shall include (without limitation) an individual retirement account, a Roth IRA, and any Retirement Plan qualified under Section 401(a) of the Internal Revenue Code.

(3) The term “minimum required distribution amount,” as it applies to an interest in any Retirement Plan, shall mean the minimum amount required to be distributed for any calendar year from the Retirement Plan with respect to that interest under the minimum distribution rules.

(4) The term “Designated Beneficiary” shall refer to an individual who is considered to be the beneficiary under a Retirement Plan for life expectancy and minimum payment rule purposes under Section 401(a)(9) of the Internal Revenue Code and the regulations thereunder, as then amended. It is recognized that a “See-Through Trust” may be the recipient of a Plan whereby the Primary Beneficiary of such trust may be considered the Designated Beneficiary for minimum distribution purposes.

(5) The term "Eligible Designated Beneficiary" shall have the same definition as defined in Internal Revenue Code §401(a)(9)(E)(ii), and the regulations thereunder, as then amended. The Grantor acknowledges that an Eligible Designated Beneficiary is an individual who is considered to be a beneficiary eligible for payment over such beneficiary's life expectancy under a Retirement Plan for minimum required distribution purposes.

(6) The term "Accumulation Trust" shall refer to any trust, which an interest in an IRA and/or Retirement Plan is owned by, payable to, or allocated to, that qualifies (or will qualify by reason of the language hereof) to have a beneficiary be treated as the Designated Beneficiary of the Retirement Plan for the purposes of the minimum required distribution rules promulgated by the Department of the Treasury thereunder, as then amended, whereby the Trustee of such trust has the discretion or an obligation to accumulate and withhold distributions to the beneficiaries of such trust, any minimum required distribution amount, or the income or reinvestment thereof, that is owned by, distributed to, payable to, or allocated to such trust.

(7) The term "Conduit Trust" shall refer to any trust, which requires by its terms that any and all distributions received from any Retirement Plan or plans must be distributed to an individual beneficiary who may be considered the Designated Beneficiary of the Retirement Plan for the purposes of the minimum required distribution rules promulgated under Section 401(a)(9) of the Internal Revenue Code, and the regulations promulgated by the Department of the Treasury thereunder, as then amended.

(8) The term "See-Through Trust" shall refer to any trust that meets the definition of either an "Accumulation Trust" or a "Conduit Trust," as defined above.

(9) The term "Inherited IRA or Retirement Plan" shall refer to any Retirement Plan, as defined in paragraph (2) above, of which the Grantor is a Designated Beneficiary, or any such Retirement Plan of which the Grantor is not considered to be a participant and/or an owner.

(10) The term "Distribution Deadline" shall refer to December 31 of the calendar year by which all assets must be distributed from a Retirement Plan pursuant to the minimum distribution rules under Section 401(a)(9) of the Internal Revenue Code and the regulations thereunder, as amended.

(b) Marital Trusts. To the extent that an interest in a Retirement Plan is owned by, payable to, or allocated to a trust (or portion of a trust) which qualifies for a marital deduction, then the following provisions shall apply, notwithstanding any provision herein to the contrary:

(1) The Trustee shall exercise all discretionary powers as beneficiary of each Retirement Plan so as to ensure that the Retirement Plan will distribute to the trust each calendar year (or portion of such calendar year) the greater of (i) the ordinary income generated by the undistributed account balance of the Retirement Plan, or (ii) the minimum required distribution amount. The Trustee may cause the Retirement Plan to distribute such additional amounts as the Trustee considers advisable.

Further, notwithstanding anything to the contrary above, any and all distributions made from a Retirement Plan held under any such marital trust shall be payable directly to the Grantor's spouse during his or her lifetime. Accordingly, any amounts withdrawn or distributed from the Retirement Plan (medical expenses properly charged thereto) shall be distributed to the Grantor's spouse forthwith and shall not be accumulated. The purpose of this paragraph is to assure that the marital trust which holds the Retirement Plan qualifies as a "Conduit Trust." Nevertheless, the requirement that any and all amounts withdrawn or distributed from a Retirement Plan be in turn distributed to the Grantor's spouse may be eliminated by action of the Qualified Plan/IRA Trust Protectors named at subsection (h) of this Section, provided that any such action may occur only on or before September 30 of the year following the calendar year of the Grantor's death.

(2) The Trustee shall pay to the Grantor's spouse, if the Grantor's spouse is living after the death of the Grantor, as beneficiary, the greater of the net income of such trust or the minimum required distribution amount in convenient installments but no less frequently than quarterly.

(3) All taxes, fees, and expenses payable by the trust (or portion) which might otherwise be chargeable against amounts distributed from the Retirement Plan shall be paid from the principal of the trust (or portion).

(4) Further, the Trustee shall follow any and all Treasury Regulations and IRS pronouncements to the extent necessary to assure that a trust intended to qualify for the estate tax marital deduction which is the recipient or holder of a Retirement Plan will be in compliance with the rules that must be followed in order to qualify for the federal estate tax marital deduction.

(c) Expense and Beneficiary Limitations. If this Trust or any separate trust established under this Trust Agreement upon or after the death of the Grantor becomes the beneficiary of any Retirement Plan, the Trustee shall administer any proceeds received from any such Retirement Plan, and the income and/or proceeds thereof, as provided in this Trust Agreement, provided, however, that no federal or state estate, inheritance or other taxes nor any debts, liabilities, last expenses, administrative costs, or other charges (except for legitimate administrative expenses of the applicable separate trust itself which are incurred after funding thereof) may be paid from such trust, or the proceeds of any Retirement Plan. Further no assets held under such trust that is funded by or is the beneficiary of a Retirement Plan may be transferred to any other Trust or merged with any other Trust that would result in a non-individual, being a beneficiary thereof, and no fiduciary or Trust Protector shall have the right to exercise any power that would violate the Designated Beneficiary rules under the rules promulgated under Section 401(a)(9) of the Code, and the regulations promulgated by the Department of the Treasury thereunder, as then amended. Additionally, if an Eligible Designated Beneficiary is the Designated Beneficiary of the applicable trust, then no assets held under such trust that is funded by or is the beneficiary of a Retirement Plan may be transferred to any other trust or merged into a trust that would result in an individual older than such Eligible Designated Beneficiary being a beneficiary thereof.

(d) Power of Appointment Limitations. Notwithstanding any provision granting a Power of Appointment under this Trust Agreement, any Power of Appointment that may be exercised to appoint or affect the disposition of Retirement Plan proceeds, or the income, proceeds of distribution, or reinvestment thereof, shall be exercisable solely in favor of individuals. Also, any general Power of Appointment to appoint assets held under such a trust (or any plan, rights, or the proceeds of investment thereof) to the power holder's creditors or creditors of the power holder's estate shall instead be construed to be a power to appoint such proceeds only to creditors of the power holder who are individuals. Further, in addition, if any such trust is held for the primary benefit of an Eligible Designated Beneficiary, and such trust allows for the payment of Required Minimum Distributions over the life expectancy of an Eligible Designated Beneficiary pursuant to Section 401(a)(9) of the Code and the regulations thereunder, then under no circumstances shall any individual older than such Eligible Designated Beneficiary be eligible to be a potential appointee under any Power of Appointment set forth herein.

(e) Shadow Trust Provision. The Trustee is advised to maintain separate accounts for Retirement Plan proceeds and other trust assets to assure compliance with this Section and may request a court order to the effect that there will be a separate "shadow" trust established to hold any and all Retirement Plan distributions in a manner equivalent to how the trust would have been held if such separate trust had not been established, except for the changes with respect to the governing rules that apply to such separate trust, as required by this Section. The primary purpose of the establishment of such a shadow trust may be to permit the originally named trust herein established to be administered with respect to non-Retirement Plan assets without being subject to requirements of this Section. If such a trust is established by court order then the requirements of this Section will apply only to such separate established shadow trust.

(f) Divided Trust Provision. As to any trust herein established which benefits a Primary Beneficiary and may qualify as an Accumulation Trust or Conduit Trust with respect to such Primary Beneficiary but for providing payments or benefits to one or more non-individual beneficiaries, the Trustee is authorized to divide any such trusts into two separate trusts, one of which may be the recipient of Retirement Plan assets and/or rights, and shall not be permitted to pay any distribution or benefits to any non-individual beneficiary, with the other trust or trusts to be funded with non-Retirement Plan assets and to be used for the benefit of such individuals and/or non-individual beneficiaries as by its terms would otherwise apply. In addition, the Trustee is authorized to divide any trust herein established which benefits an Eligible Designated Beneficiary so that a separate trust would be established for the benefit of such Eligible Designated Beneficiary, and no assets shall be distributed to or for the benefit of any non-individual beneficiary or to any individual older than the Eligible Designated Beneficiary, with the other trust or trusts to be funded with assets as set forth above.

(g) Contingent Beneficiary Alteration. If this Trust or any separate trust established therefrom becomes the beneficiary or receives the proceeds from any Retirement Plan, then upon the death of a Primary Beneficiary who is the Eligible Designated Beneficiary with respect to such Retirement Plan, if the remaining trust assets are not effectively appointed under a Power of Appointment herein established or devised outright or in separate trusts solely for descendants of the Grantor on a per stirpes basis, then the Trustee shall divide the separate trust into separate equal shares, per stirpes, for any individual heirs at law that would take such property under the applicable state intestacy statute who are younger than such deceased Primary Beneficiary, provided that any such heirs at law who are older than such Primary Beneficiary who is an Eligible Designated Beneficiary and any non-individuals shall be considered as deceased or not in existence for the purposes of this paragraph and shall not be permitted to receive any distribution of a Retirement Plan or any assets therefrom. As a result, no distribution of a whole or part of a Retirement Plan, of which this Trust or any separate trust established therefrom is a beneficiary, shall occur upon the death of Primary Beneficiary who is the Eligible Designated Beneficiary with respect to such Retirement Plan other than a distribution to an individual who is younger than such deceased Primary Beneficiary pursuant to the applicable then current State law of distribution or the intestacy statute or as appointed under any Power of Appointment herein provided. Notwithstanding any provision herein to the contrary, the only beneficiaries of any Trust which is to receive Retirement Plan proceeds or to be the beneficiary of a Retirement Plan shall be appointees under a Power of Appointment exercised subject to the terms of this Agreement, any personal descendants, and any individual heirs at law who are younger than such Primary Beneficiary, as determined by the then current state intestacy statute, or trusts for their benefit which qualify as a "See-Through Trust," as defined in this Section; provided, however, the class of beneficiaries of any trust which is to receive Retirement Plan proceeds or be the beneficiary of a Retirement Plan shall be further limited if the Primary Beneficiary is an Eligible Designated Beneficiary so that no individuals who are older than the Primary Beneficiary who is an Eligible Designated Beneficiary shall not be entitled to receive any benefits from any such Retirement Plan or trust.

(h) Applicable Multi-Beneficiary Trust Language. Notwithstanding anything to the contrary in Article Four or Article Five of this Trust Agreement, if the Primary Beneficiary of a trust established upon the death of the last surviving Grantor is "chronically ill" [as such term is defined in Code Section 401(a)(9)(E)(ii)(IV)] or "disabled" [as such term is defined in Code Section 401(a)(9)(E)(ii)(III)], then, during the lifetime of such Primary Beneficiary, no distributions from the separate trust established for the primary benefit of such Primary Beneficiary shall be made to any individual or entity other than the Primary Beneficiary and such separate trust shall be held, managed and administered for the sole lifetime benefit of such Primary Beneficiary and no other individual other than such Primary Beneficiary; provided, however, that distributions from such separate trust may be made to an individual other than the Primary Beneficiary only if such other individual is an Eligible Designated Beneficiary and only to the extent that distributions to or for the benefit of such other individual who is an Eligible Designated Beneficiary prior to the death of the Primary Beneficiary do not disqualify such separate trust from being an "applicable multi-beneficiary trust" which permits the required minimum distributions to be made over the life expectancy of the Primary Beneficiary pursuant to Code Section 401(a)(9)(H)(iv). The purpose of the preceding sentence is to permit any such separate trust established for a Primary Beneficiary who is chronically ill or disabled to be a "applicable multi-beneficiary trust" pursuant to Code Section 401(a)(9)(H)(iv) to enable required minimum distributions with respect to any Retirement Plan which are held by or made payable to such separate trust to be made pursuant to the life expectancy of such Primary Beneficiary. Further, no distributions may be made to or for the benefit of such Primary Beneficiary unless such distribution is permissible pursuant to the special needs distribution standards set forth in Section 5.02 of this Trust Agreement, if and when applicable, and the Trustee shall further have the power and authority to completely withhold any and all distributions or benefits for such Primary Beneficiary in the Trustee's sole and absolute discretion. [THIS IS OPTIONAL "AUTO-SWITCH" LANGUAGE WHERE AN ACCUMULATION TRUST WOULD AUTOMATICALLY BE ESTABLISHED UPON THE DEATH OF THE GRANTOR IF THE PRIMARY BENEFICIARY IS CHRONICALLY ILL OR DISABLED]

(i) Qualified Plan/IRA Trust Protector Powers. ____________________ (or if left blank, GASSMAN, CROTTY & DENICOLO, P.A.) is hereby appointed as Qualified Plan/IRA Trust Protector and shall have the authority to make amendments to this Trust Agreement and with respect to any trust herein established which benefits a Designated Beneficiary after the Grantor's death for the purpose of: (1) qualifying any such trust as an Accumulation Trust or as a Conduit Trust as described herein under subsections (a)(5) and (6) hereof; or (2) allowing for the payment of Required Minimum Distributions over the life expectancy of an Eligible Designated Beneficiary (if available), with such modifications to be effective as of or before September 30th of the calendar year following the calendar year of the Grantor's death. Notwithstanding the above, no changes may be made by a Qualified Plan/IRA Trust Protector in any manner that would cause loss of qualification for the Federal Estate Tax Marital Deduction with respect to any marital devise or devise in trust to or for the benefit of the Grantor's spouse that would qualify for the Federal Estate Tax Marital Deduction.

(j) Documentation Requirements. In order to comply with the documentation requirements of Treasury Regulation §1.401(a)(9)-4, Q&A-6, the Trustee is required to provide either the Plan Administrator or Trustee of the Retirement Plan account or accounts a copy of this Trust Agreement, a list of all beneficiaries of the Trust, including contingent and remaindermen beneficiaries, with a description of the conditions on the entitlement, no later than October 31st of the calendar year following the calendar year of the Grantor's death, and to certify that to the best of Trustee's knowledge, the list is correct and complete, as of September 30th of such year, and that the requirements of Treasury Regulation §1.401(a)(9)-4, Q&A-6(b), or any subsequent regulations, are satisfied; provided, however that the Trustee may elect not to provide such documentation if as a result of not providing such documentation the Trust would be eligible for a more favorable payout method under the minimum distribution rules.

THE FOLLOWING LANGUAGE CAN BE USED TO IMPLEMENT THE TEA POT TRUST SYSTEM UNDER A TRUST AGREEMENT TO WHICH IRA/PLANS ARE MADE PAYABLE:

TEA POT Trust Provisions. Any and all Qualified Retirement Plans other than Roth IRAs and other Roth Retirement Accounts that are not taxable when withdrawn that are payable to this Trust shall be held, managed, and administered pursuant to the CLIENT QUALIFIED BENEFITS TRUST as set forth in this Section ______ [NUMBER OF THE SECTION WHERE THIS PROVISION WILL BE ADDED] of this Trust Agreement. The trusteeship set forth in Section _____ [THE SECTION ADDRESSING TRUSTEESHIP] of this Trust Agreement shall apply to the CLIENT QUALIFIED BENEFITS TRUST and CLIENT EQUALIZATION TRUST established under this Section. It is my intention that such trusteeship shall continue until the end of the tax year that is at least eleven (11) years after my death as to any such Qualified Retirement Plans, notwithstanding that other assets are intended to be transferred into separate trusts with different trusteeship which may allow each of my children to serve as a Trustee or change the trusteeship of such separate trusts for their benefit.

The CLIENT QUALIFIED BENEFITS TRUST shall be held, managed, and administered as provided in this Section, and the Trustee thereof may distribute income and/or principal of the assets of such Trust to or for the health, education, maintenance and support of any or all of my descendants or to Trusts that benefit one or more descendants as the Trustee deems appropriate in the Trustee's discretion, taking into account that for planning purposes, it may be best to have one or more of my descendants receive distributions from such Trust, based upon the most effective income tax planning as determined by such Trustee(s). Notwithstanding the above, any Qualified Retirement Plan, or account or right associated therewith, that can be paid out without generating income tax may also be allocated to such CLIENT QUALIFIED BENEFITS TRUST, or to the separate trusts established for my descendants under Section ____ [THE SECTION ADDRESSING DIVISION OF ASSETS INTO SEPARATE TUSTS FOR DESCENDANTS OR OTHER BENEFICARIES] this Trust Agreement, as deemed appropriate in the discretion of the Trustee(s). Further notwithstanding anything to the contrary in Section ____ [THE SECTION ADDRESSING THE DIVISION OF ASSETS INTO SEPARATE TRUSTS FOR DESCENDANTS AND/OR OTHER BENEFICARIES] the Trustee(s) shall fund the CLIENT EQUALIZATION TRUST with an amount at least equal in value (as of the date of funding) to the amounts of taxable Qualified Retirement Plan assets that will be payable to the QUALIFIED BENEFITS TRUST. The purpose of the CLIENT EQUALIZATION TRUST will be to enable the Trustee(s) thereof to make distributions of monies or assets that are not received from the CLIENT QUALIFIED BENEFITS TRUST in order to help assure that, if one or more of my descendants have the benefit of receiving more payments than others, or earlier payments as opposed to later payments, under the CLIENT QUALIFIED BENEFITS TRUST, then the CLIENT EQUALIZATION TRUST assets can be used to "even up" inheritances. Accordingly, the Trustee may distribute income and/or principal of the assets of such CLIENT EQUALIZATION TRUST to or for the health, education, maintenance and support of any or all of my descendants, and to one or more 501(c)(3) charities if and when requested by descendants and deemed to be appropriate in the discretion of the Trustee, and distributions may be made to the separate irrevocable trusts being established for my descendants under Section _______ [THE SECTION ADDRESSING THE DIVISION OF ASSETS INTO SEPARATE TRUSTS FOR DESCENDANTS AND/OR OTHER BENEFICARIES], as the Trustee deems appropriate in the Trustee's discretion, in order to achieve this objective. The Trustee of the CLIENT EQUALIZATION TRUST is encouraged to hold the Trust assets, and to not make distributions until after the CLIENT QUALIFIED BENEFITS TRUST assets have been distributed in full, unless otherwise advised by legal or tax counsel after careful consideration. At that time, the Trustee of the CLIENT EQUALIZATION TRUST is encouraged, but not required, to make distributions to the trusts established under Section _______ [THE SECTION ADDRESSING THE DIVISION OF ASSETS INTO SEPARATE TRUSTS FOR DESCENDANTS AND/OR OTHER BENEFICARIES] of the Trust Agreement so that the net after tax distributions received by the Primary Beneficiary of the applicable trust established under Section _______ [THE SECTION CONTAINING THE LANGUAGE WHICH GOVERNS THE SEPARATE TRUST ESTABLISHED FOR A PARTICULAR BENEFICARY] and other beneficiaries of each trust have been taken into account, and treated fairly with charitable contributions that have been made at the request of one or more beneficiaries to be considered as having been made to such beneficiaries for purposes of equalization.

Payments made from the CLIENT QUALIFIED BENEFITS TRUST after September 30 of the calendar year following the year of my death may be made only to my descendants, trusts for the sole and exclusive benefit of my descendants, or other individuals specifically approved in advance, in writing by my descendants, provided that, under no circumstances shall any assets held under the CLIENT QUALIFIED BENEFITS TRUST be distributed or paid to or for the benefit of any non-individual or in any way that would cause disqualification of the Trust from being a "See-Through Trust" under Internal Revenue Code Section 401(a)(9). Further, the CLIENT QUALIFIED BENEFITS TRUST shall be subject to the terms of Section _________ [THE SECTION CONTAINING LANGUAGE WHICH APPLIES TO HELP ASSURE THAT ANY TRUST WHICH RECEIVES AN IRA/PLAN WILL QUALIFY AS A SEE-THROUGH TRUST-THIS LANGUAGE IS SET FORTH ABOVE IN THIS APPENDIX H]. If a descendant of mine requests that a distribution from the QUALIFIED BENEFITS TRUST be made to a bona fide 501(c)(3) charity before such September 30th, then the Trustee(s) shall have the authority to make such distribution as the Trustee determines appropriate in its sole and absolute discretion (which may be withheld absolutely), and to reduce subsequent distributions that might otherwise be made for such requesting child or any trust herein established for such requesting child.

In addition to the above, if any beneficiary of this Trust qualifies on my date of death as "Chronically Ill" (as defined under Code Section 7702B(c)(2)), or a "Disabled" (as defined under Code Section 72(m)(7)) (any such beneficiary shall be termed a "Special Beneficiary"), then a separate portion of the Qualified Retirement Plan that would have passed to the CLIENT QUALIFIED BENEFITS TRUST may pass instead to a dedicated CLIENT TEA CUP TRUST, which may enable such Special Beneficiary to have the benefit of Qualified Retirement Plan "stretch payout rules" that presently exist for Eligible Designated Beneficiaries, as defined by Internal Revenue Code Section 401(a)(9)(E)(ii). Such a CLIENT TEA CUP TRUST shall have the same trusteeship that shall apply for the CLIENT QUALIFIED BENEFITS TRUST and the CLIENT EQUALIZATION TRUST, and shall be drafted to qualify as a "Accumulation Trust" pursuant to Internal Revenue Code Section 401(a)(9) and the applicable Treasury Regulations thereunder for the purpose of allowing the Trustee to take distributions out over the life expectancy of the Chronically Ill or Disabled Beneficiary. Further, the CLIENT TEA CUP TRUST shall be subject to the terms of Section _________ [THE SECTION CONTAINING LANGUAGE WHICH APPLIES TO HELP ASSURE THAT ANY TRUST WHICH RECEIVES AN IRA/PLAN WILL QUALIFY AS A SEE-THROUGH TRUST-THIS LANGUAGE IS SET FORTH ABOVE IN THIS APPENDIX H]. The Trustee of the CLIENT TEA CUP TRUST may distribute income and/or principal of the assets of such Trust to or for the health, education, maintenance and support of any or all of my descendants as the Trustee deems appropriate in the Trustee's discretion; provided, however, that no distributions may be made to or for the benefit of a Special Beneficiary unless such distribution is permissible pursuant to the special needs distribution standards set forth in Section ___________ [THE SECTION SETTING FORTH SPECIAL NEEDS TRUST PROVISIONS THAT APPLY TO A TRUST ESTABLISHED FOR

A BENEFICARY WHO IS RECEIVING OR MAY RECEIVE GOVERNMENTAL ASSISTANCE] of this Trust Agreement, if and when applicable, and the Trustee shall further have the power and authority to completely withhold any and all distributions or benefits for such Special Beneficiary in the Trustee's absolute discretion. The Trustee of the CLIENT QUALIFIED BENEFITS TRUST and the CLIENT TEA CUP TRUST shall make such distributions as they determine to be appropriate to take into consideration my general desire that each child of mine and his or her respective descendants would benefit in an equivalent manner under this Trust Agreement. To confirm such intent by example, if I were to die with two children, with one having two of his or her own children and one having one of his or her own children, then it is my general desire that 50% of all assets and benefits will pass in trust for the first child and to his or her descendants, and that 50% will pass in trust for the other child and his or her present and future descendants, notwithstanding that my children may have different needs, earning ability and potential catastrophic circumstances.

Within a reasonable time after all distributions have been made to the CLIENT QUALIFIED BENEFITS TRUST from any Qualified Retirement Plan payable to such trust, the Trustee may distribute some or all of the remaining Trust assets to the separate trusts established for my descendants, which are formed pursuant to Section _______ [THE SECTION CONTAINING THE LANGUAGE WHICH GOVERNS THE SEPARATE TRUST ESTABLISHED FOR A PARTICULAR BENEFICARY], in such proportions as the Trustees deem to be appropriate, taking into account what beneficiaries of such trusts have received before such trust is distributed.

Notwithstanding the above, any _____ of my children, voting together, may require the Trustee to reduce the amounts being set aside in one or more of the trusts above, or require that all assets be divided into equal shares for each of my children, per stirpes, provided that they have consulted with independent and qualified legal counsel and a reputable certified public accountant before any such decision is made.

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Alan S. Gassman, J.D., LL.M. is a board-certified estate planning and trust lawyer who practices in Clearwater, Florida. He has an LL.M. in taxation from the University of Florida, and practices in the areas of trust and estate planning, taxation, wealth preservation, and the representation of physicians and medical practices.

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Index

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