BEST MONTHLY WEBINAR

IRA
Beneficiary Planning

Presented by:

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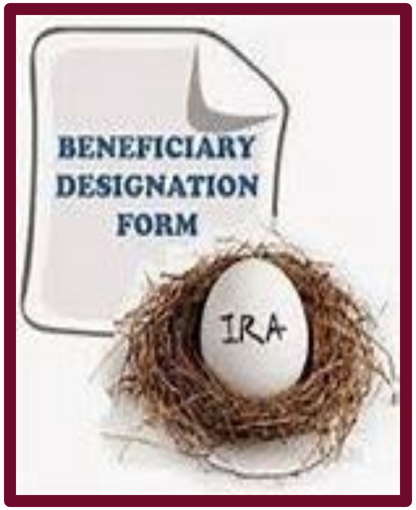
Our Agenda

- Importance of IRA Beneficiary Planning
- Various Beneficiary Designation Options
- IRA Beneficiary Planning Strategies



Importance of IRA Beneficiary Planning

- Strengthen relations with clients
- Reduce income taxes and estate taxes, and
- Ensure that the family's financial legacy passes properly to the next generation

Role of Advisor

- Review beneficiary designation forms regularly with your clients
    - CFO of your client's assets during their lifetime and after their deaths for the benefit of their beneficiaries
- Don't take forms for granted
    - Become knowledgeable of your custodial/trust agreements (default provisions).
- Forms must be coordinated with your client's estate planning objectives.

FINRA Rule 2090 requires every FINRA member firm to "use reasonable diligence, in regard to the opening and maintenance of every account, to know (and retain) the essential facts concerning every customer and concerning the authority of each person acting on behalf of such customer."

IRA Custodial Forms

- Does your custodian allow for the designation of per stirpes or per capita?
- Does your custodian automatic disqualify a divorcing spouse as a beneficiary?
- Does your custodian allow for successor beneficiaries to be named by the participant and/or the beneficiary?
- Does your custodian allow for the “automatic” set-up of separate accounts after the participant’s death?
- Does your custodian allow for custom designated beneficiary forms?

IRA Beneficiary Form Mistakes

- No Beneficiary Form On File
- No Contingent Beneficiaries
- Outdated Forms (Former Spouse, Etc.)
- Financially Irresponsible Beneficiaries
- Naming Trust Or Estate As Beneficiary

IRA Beneficiary Planning

- IRA participant (owner) has the right to name whoever they wish to be the beneficiary of their IRA.
  - Five basic options: Spouse, if married; children, grandchildren, or other individuals; a trust; a charity; or some combination of the above.
    - IRC does not take community property laws into consideration for federal tax purposes (PLR 201623001)
- IRA Beneficiary:
  - The person or persons who inherit the IRA after the participant’s (owner’s) death. Must be named prior to death (Revocable vs. Irrevocable)
    - Primary and a Contingent beneficiary should always be used. (All My Children, Per Stirpes, Per Capita)
- “Designated Beneficiary” rules vs. No “Designated Beneficiary rules.”

Designated Beneficiary (DB)

- Who is a Designated Beneficiary? [IRC § 401(a)(9)(E)]
    - Any individual (a natural person)
    - A “qualifying” trust (see-through/conduit trust)
    - Multiple beneficiaries (if, they meet separate account requirements
- What is the importance of a Designated Beneficiary?
    - Provides favorable life expectancy of the beneficiary pay-out method (“Stretch-out”)
- DB Finalization Date
    - September 30 of the year following the IRA participant’s death [Treas. Reg. 1.401(a)(9)-4 Q&A 4].

Spouse Designated Beneficiary

- Designating the spouse as the primary DB may prove to be the best and easiest planning method.
- It is not essential that the Spouse be the "sole designated beneficiary" (primary beneficiary) at the time of the participant's death:
  - Only that she is a beneficiary on the date of death, and
  - She is *"sole designated beneficiary"* of the entire account by the "designated beneficiary finalization date."
    - September 30 of the year following the death of the IRA participant.
- Remove (cash-out) other named beneficiaries; disclaim or fund separate accounts by 12/31 of the year following the year of the death of the participant.

Spouse Designated Beneficiary

Death of Participant Prior to RBD

- Lump sum
- Rollover to new or existing IRA
  - Year in which he/she reaches their RBD (Uniform Lifetime Table)
- Remain as a beneficiary (Inherited IRA)
  - No RMDs required until the deceased spouse would have reached age 70 ½
  - Single Life Table (Recalculated)
  - No 10% penalty

Death of Participant After RBD

- Lump Sum
- Defer for 5 years
- Rollover to new or existing IRA
  - Year in which he/she reaches their RBD (Uniform Lifetime Table)
- Remain as a Beneficiary (Inherited IRA)
  - RMD in year the deceased spouse would have reached age 70½
  - Single Life Table (Recalculated)
  - No 10% penalty

Spouse Remains As A Beneficiary

- Two Reasons:
  - Surviving spouse is older than 70½ and the deceased spouse was younger than 70½
  - Surviving spouse is under age 59½ and needs the IRA funds
- Remain as a beneficiary:
  - No RMDs required until deceased would have reached age 70½
  - Not subject to the 10% early (pre-mature) distribution penalty
  - Rename successor beneficiaries
- Remaining a beneficiary has no effect on the surviving spouse's ability to do a rollover later on.
  - Rename beneficiaries (allowing the L/E choice for beneficiaries)

Non-Spouse Designated Beneficiary

Death of Participant Prior to RBD	*Death of Participant After RBD*

• Lump sum
• 5–Year deferral
• Life expectancy of beneficiary (default protection)
• Distributions must begin:
  ○ 12/31 year after year of participant's death
  ○ Single life table w/fixed term method (reduce by one each year)
	• Lump sum
	• Life expectancy of beneficiary (default protection)
	• Distributions must begin:
	  ○ 12/31 year after year of participant's death
	  ○ Single life table w/fixed term method (reduce by one each year)

Single Lifetime Table For Inherited IRAs

Single Life Expectancy Table (Minimum Distribution Incidental Benefit Table)			
Age	Applicable Divisor	Age	Applicable Divisor
10	72.8	60	25.2
20	63.0	61	24.4
25	58.2	62	23.5
30	53.3	63	22.7
35	48.5	64	21.8
40	43.6	65	21.0
41	42.7	70	17.0
42	41.7	71	16.3
43	40.7	72	15.5
44	39.8	73	14.8
45	38.8	74	14.1
46	37.9	75	13.4
47	37.0	80	10.2
48	36.0	85	7.6
49	35.1	90	5.5
50	34.2	95	4.1
51	33.3	100	2.9
52	32.3	110	1.1
53	31.4	111+	1.0
54	30.5		
55	29.6		
56	28.7		
57	27.9		

*Use this table if your beneficiary is someone other than your spouse.

Source: IRS Publication 590

Non-spouse IRA Rollovers

- Section 829 (a)(1) of the Pension Protection Act of 2006 (PPA '06) added IRC Sec. 402(c)(11), to allow rollover distributions to an inherited IRA of a non-spouse
- Eligible retirement plans include:
  - Qualified plans (IRC § 401(a)(1)
  - IRC § 403(a) and (b) annuities, and
  - IRC § 457 plans
- Must be established through trustee-to-trustee transfer (treated as an Inherited IRA)
- RMD must be taken by 12/31 of the year following the year of participant's death for L/E payout option (if not 5-year rule)

No Designated Beneficiary

- No name on beneficiary designation form
- Trust (non-qualifying as a DB)
- Not an individual:
  - Estate
  - Charitable organization
- Result: Lose the ability to use beneficiaries life expectancy (loss of “stretch-out”)

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No Designated Beneficiary

Death of Participant Prior to RBD	*Death of Participant After the RBD*

• Lump sum
• 5 year rule
	• Lump sum
	• Use remaining life expectancy of deceased participant (based on age at year of death).
	  ○ Distributions must begin by 12/31 of the year following the year of participant's death
	  ○ SL table (minus one each year)

NO DB vs. DB w/Life Expectancy Rule

Year	Immediate Distribution	5-Year Distribution (No DB)	Distribution to DB
5	$409,100	$434,268	$706,866
10	$557,876	$592,197	$983,022
15	$760,757	$807,559	$1,355,782
20	$1.037,418	$1,101,241	$1,852,480
25	$1,414,692	$1,501,725	$2,503,916
30	$1,929,168	$2,047,852	$3,341,253
35	$2,630,742	$2,792,587	$4,389,123
40	$3,587,454	$3,808,157	$5,652,011

Note: Assumes the deceased IRA participant died at age 68 and the beneficiary is 38 y.o. IRA balance is $500,000 . A growth rate of 8% and a 40% combined federal and state income tax rate on the IRA distribution. Source: Michael Keebler; The "IRA Inheritance Trust™".

Multiple Beneficiaries

- The most controversial area under the final regulations
- If all are individuals, the applicable distribution period (ADP) is the life expectancy of the **e<u>ldest</u>** designated beneficiary (shortest life expectancy)
- Exception: Divide into separate accounts by DB finalization date (cash out)
  - September 30 of the year following the death of the IRA participant.

Separate Accounts

- Must allocate all post-death investment gains and losses, contributions, and forfeitures on a pro rata basis
  - Then each separate account must be "funded" by 12/31 of year after year of death to determine the ADP
- Each individual beneficiary (DB) could then make his/her own decision:
  - Lump-sum
  - 5-year rule, or
  - Life expectancy

Trust As Beneficiary

- Leaving an IRA to a trust is sometimes desirable:
  - Estate planning, family, control, investment and allowances for discretion reason that trusts (properly drafted) are generally used for:
    - QTIP Marital Trusts;
    - Bypass Trust ($11.2 million in 2018);
    - Special needs trust;
    - Forcing the L/E distribution method; and
    - Creditor protection
- Disadvantage the Trust is a No DB - tax-deferral is often reduced unless the Trust is set-up as either a:
  - See-through Trust, or
  - Conduit Trust
- Note: The income tax treatment will often be less favorable than naming beneficiaries outright (>$12,501 @37% in 2018)

See-Through Trust

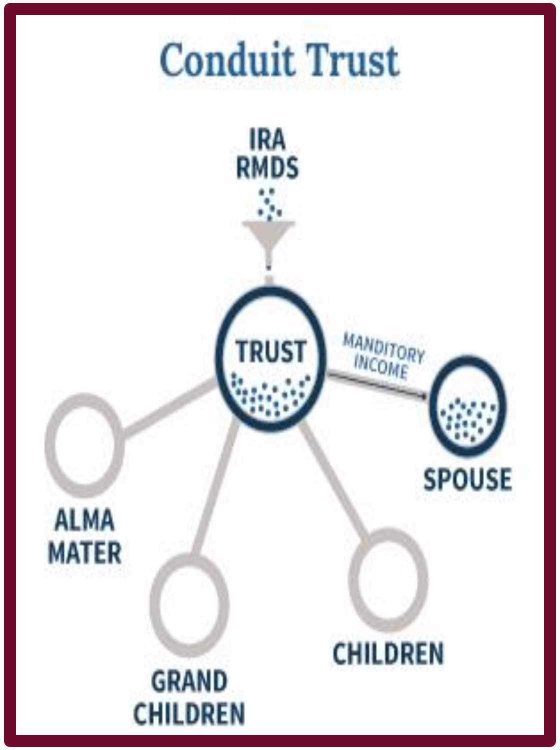
- Allows RMDs to be paid out over the L/E of the "**eldes**t" trust beneficiary using the S/L Table w/fixed term method, or
- Over the single L/E of each trust beneficiary if a separate sub-trust is named for each trust beneficiary named on the DB form
  - Spouse named as Trust beneficiary loses the ability of spousal rollover option
- Funds can be accumulated in the trust
  - Trust income taxed at highest individual tax rate 37% on income over $12,501 in 2018 (plus 3.8% on NII)
  - Also may be subject to state trust/estate tax

See-Through Trust Qualifications

- Under IRC § 401(a)(9) regulations, there are four basic requirements for a trust to qualify as a DB trust [Treas. Reg. 1.401(a)(9)-4, Q&A(5)(b)(1)]:
  - Trust must be valid under state law [Treas. Reg. 1.401(a)(9)-4, Q&A 5(b)(1)].
  - Trust is ***irrevocable or becomes irrevocable upon death of the participant*** [Treas. Reg. 1.401(a)(9)-4, Q&A 5(b)(2)].
  - Trust beneficiaries must be clearly identifiable within the trust instrument [Treas. Reg. 1.401(a)(9)-4, Q&A 5(b)(3)].
  - Trust documentation described in Treas. Reg. 1.401(a)(9)-4, Q&A 6 has been provided to the plan administrator, no later than October 31 of the year following the year of participant's death [Treas. Reg. 1.401(a)(9)-4, Q&A 5(b)(4)].

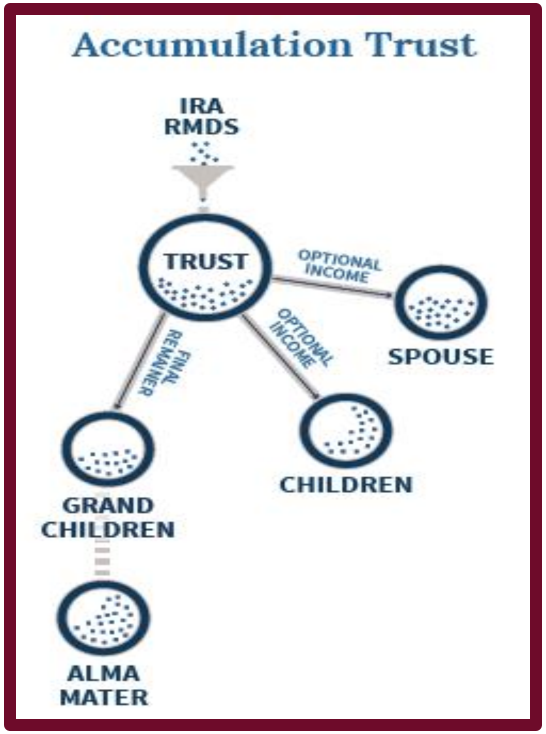
Conduit Trust

- Trust instrument must require the trustee to distribute to an individual trust beneficiary any distributions the trustee receives from the IRA
- Trustee cannot accumulate funds in the trust
- For RMD purposes, conduit trust beneficiary is treated as if he or she had been named individually as the sole DB
- Spouse named as conduit trust beneficiary, the RMDs would be paid out over his or her L/E using the SL table but w/recalculation (lose the ability of the Spousal rollover)



Accumulation Trust

- The RMD (or other distributions) is distributed from the IRA to the trust, but, the trustee has the option to "hold" the distribution and accumulate it with the principal of the trust.
  - Trust separate tax brackets
- A way to protect a beneficiary from themselves
- Can provide for all of the RMD be calculated on the age of one beneficiary, but the distributions of the RMD can be distributed out to other beneficiaries who are in lower tax brackets.



Estate as Beneficiary

- Normally, it is not advisable to designate the estate as beneficiary. Reasons why:
  - The Estate is a No Designated Beneficiary – lose choice of L/E payout distribution:
    - Lump sum
    - Five years, or
    - Remaining life expectancy of deceased participant (after 1st year, reduce by 1 every year thereafter)
  - Assets brought back through Probate
- May make sense if the IRA is small and have several beneficiaries in lower tax brackets
- PLRs: 201208039; 201736018:

Source: PLR 201736018; https://www.irs.gov/pub/irs-wd/201736018.pdf

Spouse Exception

- When the IRA doesn't name a beneficiary, the IRS has held in a PLRs that the surviving spouse can't elect to treat the IRA as his/her own because it passed through the estate rather than going directly to the surviving spouse.
  - The general rule is that even a surviving spouse who receives payments from the estate isn't allowed to roll over the distribution into his/her own IRA because the payment comes from the estate, not directly from the IRA.
- However, the IRS makes an exception if "the surviving spouse is the sole personal representative of the decedent's estate who must pay the decedent's IRA to himself as sole intestate beneficiary of the estate, and who, after such payment rolls them into an IRA set up and maintained in her name."
  - If that's the case, the portion paid to the surviving spouse can be rolled into one of his/her own IRA within 60 days without taxes or penalties to maintain the tax-sheltered growth.

Charity As Beneficiary

- Charity as sole beneficiary:
  - Income tax free
  - 100% estate tax deduction
- Charity as multiple beneficiary (No designated beneficiary):
  - Lump sum
  - Five years, or
  - Remaining life expectancy of deceased participant (after 1st year, reduce by 1 every year thereafter)
- Separate accounts by DB finalization date (cash-out)

Private Letter Rulings (PLRs)

- A private letter ruling, or PLR, is a written statement issued to a taxpayer that interprets and applies tax laws to the taxpayer's represented set of facts. A PLR is issued in response to a written request submitted by a taxpayer. A PLR may not be relied on as precedent by other taxpayers or by IRS personnel.
- PLRs aren't cheap. The standard IRS PLR fee for all IRA rulings is $10,000, and that doesn't include the professional fees you would normally incur to prepare such a ruling, which could easily run another $10,000 or more.

Source: IRS Revenue Procedure 2017-1; https://www.irs.gov/irb/2017-01_IRB

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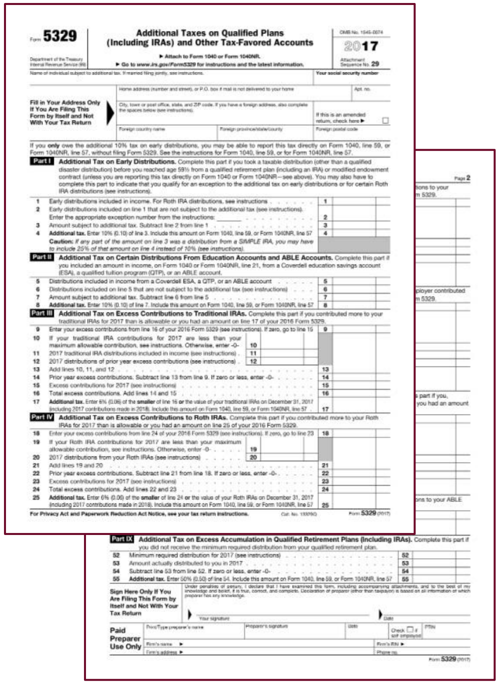
Inherited IRA

- Death after RBD taking the required RMD
  - IRS Form 5329
- Titling the account:
  - Bill Smith deceased, IRA f/b/o Mike Smith
- Inherited IRAs cannot be commingled with other IRAs
- Creditor Protection issues


Form 5329
Additional Taxes on Qualified Plans (Including IRAs) and Other Tax-Favored Accounts
2017

Inheriting an Inherited IRA

- Successor Beneficiary: “The Beneficiary’s Beneficiary”[1]
  - Most custodians allow a beneficiary to name a successor beneficiary as soon as they inherit
  - RMDs: The successor does not get to use his or her own life expectancy, but instead uses the remaining period of the original beneficiary.
- Titling the account:
  - Bill Smith deceased, IRA f/b/o Mike Smith, successor beneficiary Sara Smith

Source: [1]Ed Slott, “Successor Beneficiaries: The “Beneficiary’s Beneficiary; https://www.irahelp.com/slottreport/successor-beneficiaries-beneficiarys-beneficiary

IRA Planning Strategies

- Planning with Qualified Disclaimers
- IRC 691 - Income Respect of a Decedent
- IRA Creditor Protection (SCOTUS)

Planning With Qualified Disclaimers

- Disclaimers can be very useful in post mortem planning for retirement benefits (window of opportunity 9/21 months)
  - A refusal to accept a gift or inheritance, it is not a taxable transfer
- IRA beneficiary must be designated prior to death (primary/contingent/custom beneficiary designation form/Trust)
- Must meet certain requirements for a “qualified” disclaimer

Qualified Disclaimer Requirements [IRC § 2518]

- The disclaimer must be irrevocable
- A written disclaimer must be delivered to the “transferor of the interest”
- Must be delivered within 9 months (unless beneficiary is a child under 21)
- Accept no interest in property
- Interest must pass to next heir other than disclaimant without any direction by the person making the disclaimer

IRD Deduction

- The IRA can face a significant income tax burden as their value grows, a challenge that is only made worse for those who are subject to estate taxes on those assets as well.
- To help mitigate the combine income-and estate tax effect the IRC allows for an "Income in Respect of a Decedent (IRD) deduction [IRC § 691(c)]
- The deduction is claimed by the beneficiary (often missed)
    - File amended tax return---but only the past 3 years.
- Applies not only to inherited IRA accounts, but also other employer retirement plans, inherited non-qualified annuities, employer non-qualified stock options, deferred compensation, employer NUA stock, and more!

Spousal Rights

- Retirement Equity Act of 1984 - Federal rights granted to spouse to receive employee's pension:
  - Applies to qualified plans and 403(b) plans subject to ERISA
- IRAs, Roth IRAs and non-ERISA 403 (b) exempt from Spousal Rights under REA
- Community property law states
- State by State: Spousal Elective Share
- Custodial default provisions

IRA Creditor Protection

- Bankruptcy Consumer Abuse Protection Act 2005 (BCAPA) - Federal Bankruptcy only, does not include judgments:
  - Maximum $1,000,000 (indexed for inflation every three years) for Traditional IRAs, and Roth IRAs (2018 - 2021 = $1,321,516) [Section 522(n) of the Bankruptcy Code]
  - Unlimited protection for IRA Rollovers, SEP-IRAs, and SIMPLE IRAs
  - Unlimited protection for Self-employed Keogh or solo-401(k) plans
- State Protection:
  - State statutes vary (Opt-in/Opt-out)*
- Inherited IRAs
  - Supreme Court Ruling (Clark v. Rameker) ruled unanimously (9-0) assets held under an Inherited IRA by a non-spouse beneficiary are not "retirement funds" and therefore are not protected under **federal bankruptcy law**.
  - Several states have passed legislation to protect inherited IRAs.
    - AK, AZ, FL, IA, MO, NC, OH and TX


The End

Survey

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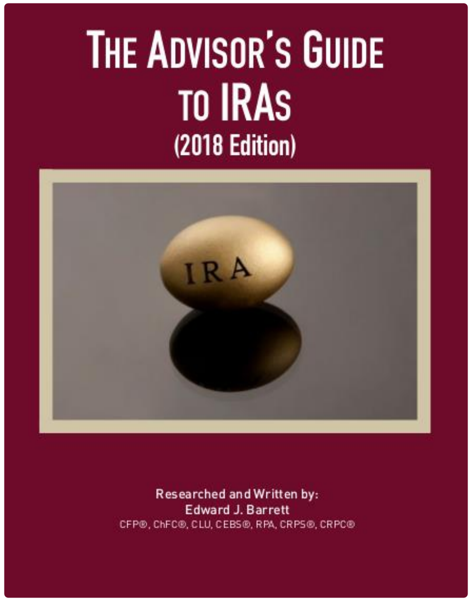

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