

Retirement Benefits Planning After the SECURE Act and the Issuance of the Proposed Regulations

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SECURE Act Background

- Setting Every Community Up for Retirement Enhancement Act.
- Enacted Dec. 20, 2019. Effective January 1, 2020.
- Eliminates stretch IRA for most beneficiaries.
- New 10-year rule.
- Careful addition to existing RMD rules: IRC Section 401(a)(9)(H).
- Retirement accounts covered: IRAs, SEPs, 401k, 403(b) plans, 457 plans, etc.
- Have become larger part of clients' balance sheets (up to 1/3 of wealth in 1 or 2 such accounts).

Retirement Plan Basics: During Life

Required Beginning Date (RBD):

- *The April 1st deadline is referred to as the participant's Required Beginning Date (RBD).*
- *RBD age was 70 ½. Now age 72. (Qualified Charitable Rollover age is still 70 ½.)*
- *Securing a Strong Retirement Act of 2022 ("SECURE 2.0"), H.R. 2954, extends RBD from 72 to 75 over a period of time.*
- *No RBD for Roth IRAs (but not Roth 401(k)s).*
- *Participant still working can delay from his employer's plan (only) if own 5% or less of employer. Retirement year is year of first RMD, with deadline of April 1 of following year.*
- *All good tax deferrals must come to an end.*

Required Minimum Distributions (RMDs):

- *How much the plan participant must take each year.*
- *First RMD must be taken by the RBD.*

50% penalty for failure to take RMD (waiver on Form 5329).

Before 59 ½, early withdrawal 10% penalty, unless exception applies (e.g., subject to certain caps, total disability, first home purchases, health insurance premiums for unemployed individuals, birth or adoption expenses, etc.).

RMD Calculations

- The following updated Tables are to be used for all RMD calculations beginning on or after January 1, 2022.
 - *If were taking distributions from an inherited retirement account prior to 2022, can use these new tables.*

Joint Life and Last Survivor Table	Used to determine RMDs for participant’s retirement account if <u>participant’s spouse is sole designated beneficiary and is more than 10 years younger than participant.</u>	Life expectancy is “recalculated” each year.
Uniform Lifetime Table	Used to determine RMDs for <u>all other participants’ accounts.</u>	Life expectancy is “recalculated” each year and is based on joint life expectancy of participant & hypothetical 10-year younger person.
Single Life Table	Used to determine RMDs for <u>beneficiaries.</u>	Life expectancy is not “recalculated,” except in the case of a surviving spouse.

Retirement Plan Basics: The Beneficiary

The Beneficiary has required minimum distributions as well.

RMD Rule depends on:

- If participant died prior to or after RBD.
- If there are multiple beneficiaries.
- The identity of the beneficiary (individual, qualifying trust, non designated beneficiary or other).

For purposes of the RMD rules, beneficiary is determined as of September 30th of year following participant's death (the “Determination Date”).

SECURE Act Changed RMD Rules for Beneficiaries

Non-Designated Beneficiaries: 5-year rule or Ghost Life Expectancy rule.

Eligible Designated Beneficiary (special individual or qual. trust): Lifetime/stretch rule.

Designated Beneficiary (all other individuals or qual. trust): 10-year rule.

Non-Designated Beneficiary Rule

No change as a result of SECURE Act.

Pre-RBD, the 5-Year Rule applies.

- Retirement benefits must be distributed no later than December 31st of the fifth year anniversary of participant's date of death.
- Annual distributions not required (e.g., all can be withdrawn in fifth year).

Post-RBD, the "Participant's Remaining LE Rule" applies.

- Distributions based on participant's remaining (hypothetical) life expectancy per Single Life Table.
 - *I.e., "Ghost Rule" or "at Least as Rapidly Rule."*

New Rule for Designated Beneficiaries

“Eligible Designated Beneficiaries” get stretch treatment over life expectancy:

1. Surviving Spouse.
2. Minor Child of the Participant (*limited stretch*).
3. Disabled Individual.
4. Chronically Ill Individual.
5. Individual no “more than 10 years younger” than Participant.

New Rule for Designated Beneficiaries (cont.)

- All other Designated Beneficiaries (other than EDBs) get 10-year rule.
- All benefits distributed by Dec. 31st of year of 10th anniversary of participant's death.

<p>If participant dies <u>before</u> her RBD:</p>	<p>No annual or periodic distributions required.</p> <p>Entire balance must be distributed by end of 10-year period.</p>	<p><i>Example:</i> Nora died on Jan. 10, 2020, <u>prior to her RBD</u>. Nora's nondisabled adult child, Remy, is her DB. Add ten years to get Jan. 10, 2030. Remy must withdraw all retirement benefits by Dec. 31, 2030 (almost eleven years after Nora's date of death).</p>
<p>If participant dies <u>after</u> her RBD:</p>	<p>RMDs must be taken in calendar years 1-9 following year of participant's death.</p> <p>RMDs calculated based on DB's life expectancy and participant's hypothetical life expectancy using <u>Single Life Table</u> (whichever is longer).</p>	<p><i>Example:</i> Nora died on Jan. 10, 2020, <u>after her RBD</u>. Nora's nondisabled adult child, Remy, is her DB. Remy, age 50, must withdraw a portion of the retirement benefits in calendar years 1-9 following the year of Nora's death. RMDs are calculated based on Remy's life expectancy under the <u>Single Life Table</u> because Remy's life expectancy is longer than Nora's hypothetical life expectancy. The balance of the retirement benefits must be distributed by Dec. 31, 2031 (the end of the tenth calendar year following Nora's death).</p>

Post-SECURE: Surviving Spouse Rules Essentially Unchanged

Option 1: Rollover to SS's own IRA.

- Can name new beneficiaries.
- Use the Uniform Life Table for calculating RMDs (smaller RMDs).
- Wait until her age 72 for RMDs.
 - *Under age 59 ½, 10% penalty will apply—maybe choose option 2 (next slide) or delay rollover until 59 ½ if need \$.*

Post-SECURE: Surviving Spouse Rules Essentially Unchanged (cont.)

Option 2: Treat as and Inherited IRA.

- Can delay RMDs until end of calendar year in which Participant would have reached 72 (or 70 ½, depending on year of death).
 - *Use Single Life Table and recalculate. RMDs will be larger than w/ rollover but smaller than for non-spouse.*
- Defined contribution plan (e.g., 401(k) or 403(b)) may provide that 10-year rule (formerly 5-year) applies if SS is sole beneficiary and does not elect LE payout.
 - *If SS does not rollover the plan, plan documents could direct that SS receives benefits as lump sum RMD, which cannot be rolled over.*
 - *Safest course of action if SS is going to delay electing LE payout: transfer plan benefits to inherited IRA outside of the plan.*
- Maybe salvage plan if paid to estate or trust with spouse as sole beneficiary. See PLRs.

Post-SECURE Differences for Surviving Spouses

Accumulation Trust for SS.

- Pre-SECURE: accumulation trust could use SS's life expectancy.
- Post-SECURE: appeared that only (i) conduit trust; or (ii) accumulation trust for chronically ill or disabled SS as of participant's death.
 - *Under Proposed Regulations, may be possible for accumulation trust for surviving spouse who is not chronically ill or disabled to qualify for LE payout if all countable beneficiaries of the trust are EDBs (see powers of appointment).*

Post-SECURE Differences for Surviving Spouses (cont.)

Treatment of successor beneficiaries of SS who elected inherited IRA option.

- If both participant and SS die before the end of the calendar year in which the participant reached age 72:
 - Pre- and Post-SECURE: SS treated as participant for purposes of determining RMDs after SS's death.
- If SS dies with an inherited IRA after participant's RBD:
 - Pre-SECURE: successor beneficiary could "step into the shoes" of the SS and continue withdrawals based on SS's distribution schedule (as if she had survived).
 - Post-SECURE: successor beneficiary must (i) continue to take annual distributions in calendar years 1-9 following the year of the SS's death based on the deceased SS's age in the year of her death; and (ii) withdraw all remaining benefits by the end of the calendar year containing the 10th anniversary of the spouse's death.
 - This 10-year rule also applies to successor beneficiaries of other EDBs and applies if a DB dies on or after Jan. 1, 2020 (even if the participant died prior to 2020).
 - Lifetime stretch option not available to successor beneficiary of an EDB who is also an EDB.

Post-SECURE Differences for Surviving Spouses (cont.)

Deadline for SS to elect to treat IRA as her own.

- Proposed Regulations impose new deadline—spousal election to treat IRA as her own must occur by later of:
 - Dec. 31 of the year after the year of the participant's death; or
 - The year in which the surviving spouse turns age 72.

- Can always rollover to surviving spouse's own IRA at a later date (other than the RMD).

Post-SECURE: Minor Child of Participant

- Completely new rule: Stretch treatment *until* the child reaches majority.
- Age of majority = 21.
- Then must distribute all benefits within 10 years (of majority).
 - *When the child's special EDB status ends, the child becomes subject to the 10-year distribution rule. Annual RMDs continue based on the child's life expectancy, with distribution of the entire account balance required by the end of the calendar year containing the child's 31st birthday.*
 - *If child dies before reaching age 21, 10-year distribution rule applies from date of child's death.*
- Does not apply to grandchildren, stepchildren, nieces and nephews.

Post-SECURE: Disabled or Chronically Ill

- Must be disabled or chronically ill **as of** the Participant's date of death.
- EDB: Receives lifetime/stretch treatment even if condition improves.

Disabled (18 or older)	<i>“Unable to engage in any substantial gainful activity by reason of . . . physical or mental impairment . . . expected to result in death or to be of long-continued and indefinite duration.”</i>
Disabled (under 18)	<i>“Physical or mental impairment that results in marked and severe functional limitations . . . expected to result in death or to be of long-continued and indefinite duration.”</i>
Chronically ill	<i>Unable to perform at least two activities of daily living or have sever cognitive impairment.</i> <ul style="list-style-type: none">• Inability to perform “activities of daily living” (ADLs) must be of indefinite duration.• ADLs: eating, toileting, transferring, bathing, dressing, continence.

Post-SECURE: Disabled or Chronically Ill (cont.)

- “Plan administrator” must be provided with **documentation** of beneficiary’s disability or chronic illness by October 31 of the year following the year of the participant’s death.
- Proposed Regulations are silent on what constitutes sufficient documentation.
- For chronically ill EDBs, documentation must include **certification** from a “licensed health care practitioner.”

ACTEC comments request:

- Alternative method for determining & documenting disability for *adult* beneficiaries
- Clarification of methods for substantiating disability for minor beneficiaries
- Extended deadline (e.g., age 21) for providing proof of minor’s disability

Post-SECURE: Individual Not More than 10 Years Younger

- Qualifies as EDB and for stretch treatment.
- Helpful in certain fact patterns: Unmarried partner, siblings.
- Based on age (not calendar year).
 - Note that this is a different rule than for determining when SS is ten years younger than the participant, which is based on birth years.

Death before RBD:

- RMDs based on the life expectancy of the EDB, however, if permitted by the plan, the EDB can elect the 10-year rule instead.

Death after RBD:

- RMDs based on the life expectancy of the EDB or the participant, whichever is longer.

Death of the Eligible Designated Beneficiary: Successor Beneficiary Rule

Distribution rule for beneficiary of the eligible designated beneficiary:

- Benefits now must be distributed within 10 years of EDB's death.
 - RMDs must continue in calendar years 1-9 following year of EDB's death based on EDB's remaining life expectancy.
 - Entire account balance must be withdrawn within 10 years of EDB's death.
- *The new "outer limit" rule applies to beneficiary who dies after Jan. 1, 2020, even if participant died pre-SECURE (retroactive application).*
- If EDB older than the participant and participant died after RBD, the entire account balance must be distributed no later than the final year of the EDB's life expectancy regardless of whether such EDB is alive or dead.
- If EDB is Surviving Spouse and Surviving Spouse dies before the end of calendar year when participant would have turned 72, then beneficiary is treated as if SS was the participant.
- No more "step in the shoes" rule.
 - *Pre-SECURE, successor beneficiary took RMDs based initial beneficiary's remaining (hypothetical) life expectancy.*

Multiple Beneficiaries of a Single Retirement Account

Default Rules:

- No DB if beneficiaries are not all individuals or qualifying see-through trusts.
- If beneficiaries are all individuals or qualifying see-through trusts:
 - Pre-SECURE: RMDs based on life expectancy of oldest beneficiary.
 - Post-SECURE: If beneficiaries are all DBs or trusts that qualify as DBs, 10-year distribution rule applies.
 - *If participant dies after her RBD, RMDs still must be taken in calendar years 1-9 following the year of the participant's death in the same manner as before over older DB's life expectancy.*

Multiple Beneficiaries of a Single Retirement Account (cont.)

Modifications to the Default Rules:

- Separate account rule: establish separate inherited IRA accounts by end of year following year of participant's death, so that each separate account is a DB or EDB
 - If each individual DB's share or EDB's share is transferred into separate account by Dec. 31 of year following year of the participant's death, the DB or EDB can use the rule that applies to it when calculating RMDs.
 - Separate share rule does not apply to trusts (except for AMBTs).
 - Life expectancy for EDBs, 10-year rule for DBs.
- Remove beneficiaries via cash-out or qualified disclaimer prior to Sept. 30th of the year following the year of the participant's death.

Multiple Beneficiaries of a Trust

Pre-SECURE: Since 2002, regulations have provided that separate account rules are not available to beneficiaries of a trust with respect to the trust's interest in the participant's benefits.

Post-SECURE: Proposed Regulations carry forward this concept.

- Separate share rule does not apply to multiple beneficiaries of a *trust* designated as retirement account beneficiary.
- *Unless applicable multi-beneficiary trust ("AMBT").*

Trusts as EDB or DB Under the Proposed Regs.

Proposed Regulations adopt terms familiar to practitioners.

“See-Through” Trust

- If the trust...
 1. Is “designated as the beneficiary of a [participant] under a plan”; and
 2. Meets the four requirements of Prop. Reg. § 1.401(a)(9)-4(f)(2) (see next slide);
- **...the underlying trust beneficiaries (not the trust itself) treated as designated beneficiaries of the retirement account.**

Conduit Trust

- All RMDs and any additional IRA withdrawals are immediately paid to trust beneficiary for life of beneficiary.
- No retirement benefits accumulate in trust.

Accumulation Trust

- RMDs and any additional IRA distributions may be accumulated or held in the trust.
- May accumulate only for benefit of Designated Beneficiaries (individuals).

NOT ALL SEE-THROUGH TRUSTS QUALIFY AS DBs.

Qualifying Trust Requirements

1. Valid under State law.
2. Irrevocable (or becomes so upon participant's death).
3. Certain documentation to plan administrator by Oct. 31st after year of death (copy of trust).
4. All trust beneficiaries who have a beneficial interest in retirement benefits held by the trust must be identifiable from the trust instrument.

If the trust satisfies these four requirements, and all countable trust beneficiaries are individuals, the trust qualifies as a DB.

RMDs are based on whichever distribution rule applies to the individual trust beneficiaries—either:

- 10-year distribution rule (RMDs required in calendar years 1-9 following year of participant's death if participant died after her RMD); or
- Lifetime stretch rules (if countable beneficiaries are all EDBs).

If the trust does not satisfy these four requirements, or all countable trust beneficiaries are individuals:

- 5-year, or “ghost” rule.

“Countable” Beneficiaries Under the Proposed Regulations

Adopts a Tier System:

1. First-Tier Beneficiaries: Current Beneficiaries of a trust at death of plan participant and any additional beneficiaries who can receive trust property prior to the death of current beneficiaries.
 2. Second-Tier Beneficiaries: Secondary beneficiaries who receive trust property at death of all First-Tier Beneficiaries.
 3. Other Secondary Beneficiaries are ignored.
- Under the Proposed Regulations, any beneficiary who **COULD** receive amounts from the trust **SOLELY** because of the death of a Second-Tier Beneficiary is not counted.
 - No more “mere potential successor” beneficiaries, BUT DOES THAT MAKE A MEANINGFUL DIFFERENCE?

Conduit Trusts Under the Proposed Regs.

Conduit Trust: A see-through trust that provides, with respect to the participant's retirement account, that "all distributions will, upon receipt by the trust, be paid directly to, or for the benefit of, **specified beneficiaries**."

- All Secondary Beneficiaries are ignored to determine countable beneficiaries
- If beneficiary is EDB: life expectancy treatment (child or spouse)
- If beneficiary is DB: 10-year rule
- Expressly recognizes conduit trust can have more than one beneficiary

Accumulation Trusts Under the Proposed Regs.

- Accumulation Trust: “any see-through trust that is not a conduit trust.”
- Qualifying Accumulation Trust: All trust beneficiaries **with a beneficial interest** in the retirement benefits (i.e., First-Tier and Second-Tier Beneficiaries“) must be **identifiable individuals (DBs)**.

Old Rule: Stretch based on age of oldest beneficiary.

New Rule:

- If all DBS or mix of DBs and EDBS (unless AMBT), 10-year rule applies.
- If participant died after RBD, RMDs required in calendar years 1-9 following the year of the participant’s death based on age of oldest countable beneficiary or participant if younger.
- Age still is relevant.
- If all are EDBS, then life expectancy rules apply.

Accumulation Trusts Under the Proposed Regs.(cont.)

First-Tier Beneficiaries	<p>“Any beneficiary would 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. . . .”</p> <ul style="list-style-type: none">➤ <i>Current or permissible distributees of the trust property upon participant’s death.</i>➤ <i>Always countable for RMD purposes.</i> <p>Note: if a beneficiary can receive trust property in any way other than resulting from the death of a current beneficiary (e.g., remarriage of surviving spouse), they are First-Tier Beneficiaries.</p>
Secondary Beneficiaries	<p>Beneficiaries that could receive amounts in the trust not distributed to a First-Tier Beneficiary at the death of the First-Tier Beneficiary.</p> <p>Certain secondary beneficiaries are countable for RMD purposes (“Second-tier Beneficiaries”). Other secondary beneficiaries are ignored.</p>

Proposed Regulations Example

Prop. Treas. Reg. Section 1.401(a)(9)-4(f)(6)(ii), Example 2.

- At death of plan participant, retirement account distributed to trust for spouse. At spouse's death, trust property distributed outright to spouse's sibling, called "A." If A dies after the participant but before spouse, then charity receives the balance of trust. Participant dies prior to RMD and spouse and A are living.
- The example concludes that the charity is disregarded, and the trust qualifies as a DB.

What if sibling did not receive trust property outright? Proposed Regulations do not address.

MY OPINION is the words "could" receive trust property "solely" because of death of Second-Tier Beneficiaries does not alter prior rules for identifying potential beneficiaries of trust property.

See Exhibit V, Section B, Item 10, where ACTEC asks the Service for clarity on this rule, taking the position that Second-Tier Beneficiaries mean the beneficiaries that receive the trust property after death of all First-Tier Beneficiaries, whether outright or in further trust.

“Countable” Beneficiaries

Until clarification, I recommend using the Outright to Now Living Person Rule to determine countable beneficiaries.

Identify all trust beneficiaries...

1. Who are alive on the participant’s date of death.
All must be individuals
2. Who would receive the retirement benefits under the terms of the trust.
3. As each beneficiary’s interest in the trust ends.
4. Until there is an outright distribution of all retirement benefits to individual(s).
All retirement benefits eventually must be distributed outright to individual(s).

Only consider individuals alive on DOD. Don’t worry about what happens if they fail to survive to receive their interest. All that matters is that they are alive on DOD.

Accumulation Trust Example

Participant Barry dies before his RBD. His IRA beneficiary is the Trust for wife, Marissa.

Trust permits discretionary distributions to Marissa during life.

At Marissa's death:

- If Eli, her only child, or his issue are living, then
 - If Eli is under 35 to Trust for Eli and if Eli dies prior to 35 or is not living, then to his issue, per stirpes, with a holdback trust for issue under age 25.
- If neither Eli nor issue is then living or die before distribution of trust property to them, then to Charity.

If Marissa and Eli survive Barry and Eli is not disabled:

- If Eli is over age 35: qualifying see-through trust—10-year payout.
- If Eli is under age 35 but above the age of 21 and has no issue living at death of Barry: trust likely fails as DB—Charity is a countable beneficiary.
- If Eli is under age 35 but above the age of 21 and has young issue: Might depend on terms of holdback trust for issue.

Accumulation Trust Example (cont.)

What if Trust permits discretionary distributions to Marissa and issue during Marissa's life?

- Both Marissa and issue are First-Tier Beneficiaries; at their death, Charity is Second-Tier Beneficiary—Trust fails as DB.
 - See Exhibit V, Section B, Item 11, where ACTEC asks the Service to consider changing the above result and treat A's issue as secondary beneficiaries.

What if at Barry's death Eli is under the age of 21 and trust otherwise qualifies as a DB.

- Special rule that if a minor child of participant is a beneficiary of an accumulation trust that counts as a DB, then trust counts as EDB and RMDs are based on the oldest beneficiary's life expectancy.
 - In Example, oldest beneficiary would be Marissa.
 - Retirement account must still be distributed within 10 years of Eli reaching age of 21 or ten years after Eli's death, if sooner.

Accumulation Trust for Disabled or Chronically Ill: “AMBT”

- Recall the general rule: no separate share treatment for beneficiaries of a trust.
- Drafters wanted to enable favorable tax treatment for trusts for disabled and chronically ill beneficiaries.
- Adopted a Newly defined term: “Applicable Multi-Beneficiary Trust” (“AMBT”). See IRC § 401(a)(9)(H)(v).
 - *Trust has more than one beneficiary.*
 - *All countable beneficiaries are DBs (i.e., individuals).*
 - *At least one beneficiary is a disabled or chronically ill individual.*
 - *Can get stretch treatment for an accumulation trust for disabled or chronically ill beneficiary.*
- SECURE drafters understood accumulation trusts.
- SECURE Act expressly permits accumulation trusts for a disabled/chronically ill beneficiary.
- Special exception- so accumulation trust for other EDBs probably not possible.
- Two types: Type I AMBT and Type II AMBT.

Accumulation Trust for Disabled or Chronically Ill: “AMBT”

Only exception to no separate share rule for trusts: “Type I AMBT,” described in Prop. Reg. § 1.401(a)(9)-4(g)(2).

- AMBT with at least one disabled or chronically ill beneficiary.
- All other beneficiaries must be DBs.
- Upon participant’s death, per trust terms, divided immediately into separate trusts for each beneficiary.
- Presumably, each separate trust analyzed separately for purposes of the RMD rules.
 - See Exhibit V, Section B, Item 13, where ACTEC asks the Service to add examples to the Proposed Regulations confirming the above.

Accumulation Trust for Disabled or Chronically Ill: “AMBT”

Type II AMBT

- Under trust terms, only one or more disabled or chronically ill individuals are entitled to trust benefits during their lifetime.
- No other individual has any right to the participant’s retirement plan benefits until the death of all such disabled or chronically ill beneficiaries.
- After the death of the of the disabled or chronically ill beneficiary, all countable secondary beneficiaries must be individuals.
- Secondary beneficiaries ignored for purposes of determining RMDs during disabled or chronically ill beneficiaries’ lifetimes.

Note: Senate version of SECURE 2.0 allows charity to be secondary beneficiary of Type II AMBT.

Drafting Special Needs Trusts For Disabled Child

Make sure Special Needs Trust does not allow distributions of retirement benefits to anyone else (e.g., issue or siblings), if you want stretch treatment.

- Typical provisions permit distributions to caretakers, companions for trips, gifts to third parties, etc. Is that a problem?
- Watch out for an early termination clause applying to retirement benefits (must be for life of beneficiary).
- See Exhibit V, Section B, Item 16, where ACTEC asks for clarity on this rule and whether payments such as the above will be considered for the benefit of the disabled beneficiary.

Age 31 Trust: A Proposed Regulations Bonus

Proposed Regulations permit a new kind of trust to qualify as a DB or EDB.

➤ *Major advance in drafting trusts for benefit of young individuals.*

If trust instrument requires complete distribution of the retirement benefits to a First-Tier Beneficiary by the earlier of...

1. the end of the calendar in which that individual attains the age of 31; or
2. the end of the year after the year of the participant's death;

...all secondary beneficiaries are disregarded for purposes of testing whether trust has only DBs or EDBs.

- Charity or an estate can be secondary beneficiaries of an Age 31 Trust.
- Same treatment as a conduit trust without forcing out distributions from the trust.
- Does a facility of payment provision cause a trust to fail to be an Age 31 Trust?

Participant's Minor Child as Beneficiary of Accumulation Trust

If participant's minor child is one of several First-Tier Beneficiaries, the participant is treated as having an EDB even if the trust has other countable First-Tier DBs who are not EDBs.

- Result: life expectancy payout based on oldest DB of the trust.
 - *May or may not be the minor child EDB*
- Retirement account benefits must be distributed from the retirement plan (but not necessarily from the trust) within 10 years of when the oldest minor child beneficiary reaches age 21 (or 10 years after such oldest minor child dies, if the child dies before reaching age 21).

Example of Minor Child + Another Beneficiary

Mary's designated beneficiary is a trust for her child, Jane, that lasts for Jane's lifetime. At Jane's death, the trust property is distributed to Mary's aunt, Louise. Mary dies before her RBD. At Mary's death, Jane, who is under the age of 21, and Louise are both living.

- The trust has a countable First-Tier Beneficiary who is a minor child of the participant.
- The retirement account qualifies for a life expectancy payout, but the life expectancy payout is based on Louise's life expectancy (because she is the oldest countable beneficiary).
- The entire retirement account balance must be distributed to the trust no later than 10 years after Jane (i) reaches age 21 or (ii) earlier dies.

The result is the same if at Mary's death the trust was for the benefit of Jane and Jane's older sister, Jill, who was 25 at Mary's death.

Example of Minor Child and Age 31 Trust

Mary's designated beneficiary is a trust for her three children. The trust provides for the general welfare of the children and when the youngest child reaches age 25, all trust property is distributed to Mary's then living children. If all the children die before the youngest child reaches age 25, the balance is distributed to charity. Mary dies before her RBD when her children are ages 16, 18 and 22.

- Since the oldest child will be age 31 when the youngest child reaches age 25, this trust should qualify as an Age 31 Trust, and charity can be ignored.
- Because the trust has a countable First-Tier Beneficiary who is a minor child of the participant, the retirement account has a life expectancy payout.
- The life expectancy payout is based on the oldest child's life expectancy (because she is the oldest countable beneficiary).

Powers of Appointment

Prop. Reg. 1.401(a)(9)-4(f)(5)(ii)(A) states:

“A trust does not fail to satisfy the identifiability requirements . . . merely because an individual (powerholder) has the power to appoint a portion of the [participant’s] interest to one or more beneficiaries that are not identifiable. . . .”

- **Broad lifetime or testamentary limited or general power of appointment appears to be permitted.**

If power is exercised or restricted in favor of one or more identifiable beneficiaries by the Determination Date (September 30 of year following the year of the participant’s death), those beneficiaries are countable beneficiaries.

If power is not exercised or restricted by Determination Date, each taker in default is treated as a beneficiary designated under the plan.

If the power of appointment is exercised after the Determination Date, then the trust is re-tested for treatment under the RMD rules for all future years taking into consideration the new identifiable beneficiary.

- Apparently, takers in default are ignored as countable secondary beneficiaries if the power has been exercised or restricted.
- See Exhibit V, Item 12, where ACTEC asks the Service for clarity on use of powers of appointment and confirmation that a trustee’s power to make discretionary distribution to beneficiaries is not considered a power of appointment.

Examples of Power of Appointment Rules Under the Proposed Regulations

Prop. Treas. Reg. § 1.401(a)(9)-4(f)(6)(iv), Example 4:

- Participant F died prior to her RBD naming a qualifying accumulation trust (Trust Q) as the beneficiary of her retirement account.
- Under the terms of Trust Q, all trust income is payable to F's surviving spouse, G, and G has a broad limited power of appointment to name the beneficiaries of the trust property in Trust Q upon G's death.
- If G does not exercise the power, then upon G's death, the trust property is distributed to F's descendants, 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 the Determination Date, 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 EDBs).
- 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 countable beneficiaries are G and G's siblings, and the default takers are ignored.
- Because all the countable beneficiaries are EDBs, annual life expectancy payments are permitted. Note, however, that a distribution of the remaining interest is required no later than 10 years after the calendar year in which the oldest of G and G's siblings dies.
- Same result if G exercises her power of appointment before the Determination Date in favor of siblings.
- Can charity be a default taker after death of G if G restricts her power before the Determination Date?

Modifications, Reformations, Decantings

- Proposed Regulations: existence of state law permitting trust modifications and decantings or the trust instrument permitting modifications and decanting will not cause the trust to fail the beneficiary identifiability test.
- A trust may be modified (e.g., through court-ordered reformation or permitted decanting) to add or remove beneficiaries by the Determination Date; such changes will be respected in determining the participant's DBs.
- As with powers of appointment, if a beneficiary is added after the Determination Date, the trust must be re-tested for purposes of RMDs in all future calendar years based on the trust terms (that now include the newly added beneficiary).

“Switch” Trusts & Drafting for Flexibility

What if unclear in drafting stage whether conduit or accumulation trust is best for the beneficiary? Whether it would be better for trust to not qualify as having only DBs?

“Switch” or “Toggle” Trust: A trust that receives retirement benefits structured as a qualifying conduit or accumulation trust, but independent Trustee or trust protector may elect to treat trust differently.

- *Elect to turn off conduit treatment in favor of accumulation trust provisions.*
- *Convert trust to Age 31 Trust.*
- *Convert trust to Last One Standing Trust.*
- *Add beneficiaries (including charity).*
- *If Participant dies at age 73 her remaining life expectancy is 16.4 years which is longer than the ten-year rule if the Trust qualifies as a DB.*

See Exhibit IV, Steven Gorin, “Drafting under the SECURE Act,” Section 11.17, beginning on p. 33 of his sample trust, for his provisions that he uses in drafting for flexibility.

Modifications after Distributions are Completed

- Trust instrument can provide that independent Trustee or trust protector can modify or decant a trust after retirement account benefits are fully distributed to the trust.
- *Does not disqualify initial trust from favorable conduit or accumulation trust treatment.*
- Of course, if retirement account proceeds are still being distributed from the retirement account, any modification that adds or removes a beneficiary will cause the trust to be re-tested.

Modification of Beneficiary Designation

- Proposed Regulations do not address modifications or reformations to beneficiary designations.
- Pre-SECURE: IRS generally refused to recognize modifications to beneficiary designations after participant's death (unless seeking spousal rollover treatment).
 - *See manuscript pp. 39-41 for PLRs dealing with retroactive reformations.*
 - *The period between death and the beneficiary determination date is a period during which beneficiaries can be eliminated but not replaced with a beneficiary not designated under the [IRA] as of the date of death.*
 - *The Service stated retroactive reformation of an instrument is not effective to change the tax consequences of a completed transaction.*
- Post-SECURE: remains to be seen whether the IRS will change its position after the issuance of the Proposed Regulations.

Unresolved Potential Drafting Issues with Conduit and Accumulation Trusts

Hold-back trusts

- If beneficiary dies prior to hold-back trust age, trust may direct distributions to beneficiary's estate which is not an individual.
- Ensure that the hold-back trust passes to individuals outright.
- Be sure trust does not violate an applicable RAP period.

Payment of debts, expenses, and taxes

- If retirement benefits can be used pay them, would IRS take the position that there is a non-individual beneficiary?
- Draft that retirement benefits can only be used prior to the Determination Date.

Dynasty trusts

- Do Prop. Regs. permit dynasty (i.e., perpetual) trusts to be DBs qualifying for the 10-year deferral period under the new tier system?
- Does it really matter?

Unresolved Potential Drafting Issues with Conduit and Accumulation Trusts (cont.)

100% grantor trusts

- May be possible for wholly owned grantor trusts (i.e., 678 trusts) to achieve DB status.

Limited withdrawal power over retirement benefits

- If trust retains retirement account distributions in trust, can beneficiary be granted a withdrawal power over retirement accounts.
- Might be used to avoid high trust income taxation rates.
- For language used by the author's firm, see Exhibit III. See also Exhibit IV, Steven Gorin, "Drafting under the SECURE Act," pages 17-18 and 45-46, for further discussion and illustration of such a power of withdrawal.

Separate trusts for retirement benefits vs. separate share

Separate Share Rule and Key Dates

- Nine months from date of death: Qualified Disclaimer deadline.
- Sept. 30th of year after death: Beneficiary Determination Date (or Finalization Date)
 - *Whoever is still a beneficiary on this date counts for determining which RMD rule applies.*
 - *Will be the five-year rule unless all beneficiaries on this date are DBs (or EDBs).*
- Dec. 31st of year after death: deadline for creating separate accounts.
- Default rule: Must consider all IRA beneficiaries for determining which RMD rule applies.
- BUT if separate accounts are created for the IRA beneficiaries by Dec. 31, RMD rules apply to benes. separately, rather than collectively (note that this date is past the Sept. 30 deadline, but division relates back for purposes of the rule).
- If ER plan requires lump sum payout and Trust counts as DB, beneficiary guaranteed right to direct rollover to IRA. Does not apply to nongovernmental 457 plan.

Post-Mortem Planning Example 1

Example: Originally, have non-Designated Beneficiary (5-year rule).

Beneficiaries of Susannah's 401(k) are:

- Frank (her husband)
- Conduit Trust for Heidi, a minor
- Charity

Post-Mortem clean-up:

- Before 9/30: Distribute charity's interest.
- Before 9/30: Roll Frank's share to IRA. Has 60-day rollover option. Now treated as sole beneficiary of his IRA.
- Conduit Trust for Heidi is only beneficiary left on 9/30.
- Result: Frank gets his own IRA. Heidi's Trust get limited stretch.
- Dangerous: Relying on charity and Frank being removed in time.

Post-Mortem Planning Example 2

Example:

Susannah's rev. trust is named beneficiary of her 401(k) acct.

Trust prohibits paying admin expenses from retirement benefits.

Has \$10k gift to Animal Charity. Remainder equally to:

1. Accumulation Trust for her husband, Frank; and
2. See-Through Accumulation Trust for John (disabled). John's siblings are lifetime beneficiaries too.

Post-Mortem clean-up:

- John's siblings sign qualified disclaimers. So John is sole life bene. and trust qualifies as AMBT on 9/30.
- Pay \$10k gift before 9/30. Charity not counted on 9/30.
- On 9/30, Rev. Trust is sole beneficiary, with one DB and one EDB.
- Using **direct** rollover, by 12/31 transfer 50% to inherited IRA for Frank's Trust and 50% to inherited IRA for John's Trust.
- Result Frank's Trust gets 10-year payout, and John's trust gets LE treatment (John's life) (AMBT).
- Don't plan to do it this way!

Putting It All Together:

Drafting Options for *Surviving Spouse*

1. Outright beneficiary designation: Nothing has changed, except successor beneficiary rule.
2. Credit Shelter Trust for Spouse:
 - If drafted as a Qualifying Accumulation Trust:
 - Spouse sole First-Tier Beneficiary: 10-year rule, and if participant died after RBD, then RMDs required in calendar years 1-9 following the year of the participant's death based on LE of participant or surviving spouse whoever is younger.
 - Sprinkle among spouse and children as First-Tier Beneficiaries: Same as above unless minor child of Participant is beneficiary, in which case LE payout based on oldest countable beneficiary with all distributions being made at the end of the calendar year when oldest minor child reaches age 31.
 - If drafted as Conduit Trust and only spouse receives RBs, LE treatment recalculated annually, and spouse can delay RMDs until end of calendar year P reaches age 72.
 - If spouse dies before end of calendar year P reaches age 72, then the spouse should be treated as the P for purposes of determining distributions to remainder beneficiaries. But see PLR 200644022 where Service held otherwise.
 - If spouse dies after the end of calendar year P reaches age 72, then RMDs required in calendar years 1-9 following the year of the spouse's death based on LE of participant or surviving spouse whoever is younger + 10-year rule.
 - Drafted as neither Conduit nor Accumulation: 5-year rule (or "ghost LE rule").
3. QTIP Trust: Net income AND all RBs (conduit language) paid to spouse:
 - LE treatment recalculated annually, and spouse can delay RMDs until end of calendar year P reaches age 72.
4. AMBT Accumulation Trust: Can use if spouse is disabled or chronically ill.

Putting It All Together:

Drafting Options for *Surviving Spouse (cont.)*

- Made planning for second marriages slightly easier:
 - *10-year payout rules applies to adult, nondisabled children in either case:*
 - Outright to spouse: Rollover to IRA with new beneficiary designations; or
 - Benefits left to conduit trust for spouse.

Putting It All Together:

Drafting options for *Minor Child /Children*

- Use a separate conduit trust for each minor child if a stretch is desired.
 - Note: *Still important to designate the conduit trust as a direct beneficiary of the retirement account. Don't designate the revocable trust.*
- For a Qualifying POT/accumulation trust:
 - If a minor child of participant is a beneficiary, then distributions based on the oldest countable beneficiary's life expectancy with all retirement accounts being withdrawn by the end of the calendar year in which the oldest minor beneficiary reaches age of 31, or by the end of the tenth calendar year after the oldest minor beneficiary dies if the oldest minor beneficiary dies before reaching age of 21, if sooner.
 - If none of the children of participant are minors, the 10-year rule will apply.
- Age 31 Trusts: Do not need to determine Second-Tier Beneficiaries.
- Nonqualifying trust: 5-year rule.

Remember:

- *The way to draft conduit and accumulation trusts has not changed significantly post-SECURE Act.*
- *Drafting accumulation trusts is easier now: A 10-year payout rule likely applies if all countable beneficiaries are individuals. An older beneficiary may not affect the payout period.*
- *Powers of appointment until exercised are ignored.*

Putting It All Together:

Drafting Options for *Minor Child/Children (cont.)*

- How important is the stretch?
- Parents of young children usually don't have large RB accounts.
- Usually 10-year rule will be okay.
- Conduit rules may be too rigid for young beneficiaries (but does allow remainder beneficiary).
 - *If okay for child to receive entire account by age 31, use Age 31 Trust.*
- Would a UTMA account work okay to receive retirement account distributions.
- Term life insurance is usually inexpensive—can help offset tax hit.
- More careful drafting required if disabled child.

Putting It All Together: Drafting Options for *Adult Child*

- Nondisabled adult Child (or any other DB, e.g., grandchild) will get same 10-year rule under:
 - Outright beneficiary designation.
 - Conduit Trust (remainder beneficiaries can be non-individuals).
 - Accumulation trust (all countable beneficiaries are individuals).
- Nonqualifying Trust: 5-year rule.
- Other considerations should drive planning (e.g., asset protection, spendthrift concerns).

Putting It All Together:

Drafting for *Disabled or Chronically Ill*

- Outright beneficiary designation: LE, but usually not a good choice.
- Conduit Trust: LE, but usually not good choice.
- *Qualifying Accumulation Trust: If AMBT, LE stretch treatment.
 - *Make sure disabled individual is sole, lifetime beneficiary. If not AMBT, 10-year rule.*
- Nonqualifying Trust: 5-year rule.

Using a CRT to Create Stretch IRA

Step 1: Make the CRT (CRAT or CRUT) the beneficiary of the IRA.

- *No income tax due when IRA pays out to CRT.*
- *Get a charitable deduction for estate tax purposes (value of remainder interest).*
- *At least 10% must pass to charity (actuarial test at beginning of trust term).*

Step 2: CRT makes annual distribution to individual beneficiary (child, for example).

- *Annual payment can be between 5% and 50%. Taxable income to individual beneficiary.*
- *With a CRUT, maximum possible term will either be either a 20-year payout or lifetime payout:*
- *Single individual trust beneficiary must be at least age 27 (approx.) to qualify for lifetime CRUT payout.*
- *Two joint lifetime trust beneficiaries would have to be at least age 36/37 (approx.).*

Step 3: At beneficiary's death, any remainder distributed to charity.

Using a CRT to Create Stretch IRA (cont.)

- Combine with life insurance on life of the individual trust beneficiary.
- Remember: Individual trust beneficiary has no access to trust principal.
- Will not necessarily result in more wealth for family (compared to an outright gift).
- Use only if client already charitably inclined, and beneficiary will have other assets available.
- Rev. Rul. 2002-20 helpful for using SNTs.

Why is This so Hard?

Discrepancy between Trust and Individual Tax Rates

Planning for distributions of retirement benefits to trusts is challenging:

1. Compressed tax rates apply to trusts: max. federal tax rate of 37% on income over \$13,450 (2022)
 2. Distributions from retirement accounts subject to ordinary income tax rates, not capital gains rates.
 3. Individuals reach max. federal rate with \$539,900 in income (single person)
or \$647,850 (married couple filing jointly) (2022 figure).
 4. Distributions held in trust can subject distributions to the maximum tax rate quickly;
 5. If RMDS are distributed to trust beneficiaries, a lower tax rate may apply.
- Understand approx. RMD size and savings resulting from distribution to beneficiary.
 - Trustee discretion is key.

Final Thoughts:

Planning Strategies Post-SECURE Act

- Understand choices and identify client goals. Give more weight to non-tax goals.
- Is there a problem to solve? Will beneficiary withdraw/need assets regardless?
- Too many variables to calculate “right” option. Don’t assume you will know income levels and tax rates.
- Roth conversions. Tricky to assess.
- Trustee selection and flexibility key. Give discretion to consider tax implications and make distributions strategically.
 - *Be mindful of how to keep distributions equitable.*
- Leaving retirement accounts to multiple family members can spread the tax burden.
 - *Perhaps don’t use a trust for all adult children in family:*
 - *Forces coordination among children and sharing of tax information.*
 - *Separate trust for each adult child and child’s issue: can sprinkle among immediate family groups.*

Final Thoughts:

Planning Strategies Post-SECURE Act (cont.)

- Consider easy solutions: Retirement to SNT or spouse or charity, other assets to other beneficiaries. Equalization?
- Could accumulation trust avoid state income tax?
- Consider partial gift/disclaimer of RBs to child at first spouse's death: May get 2 10-yr periods (at 1st and at 2nd death)
- Time withdrawals for low-income tax years or years with substantial offsetting deductions
- Post-Death administration and decisions will be key. Understand key dates
- Keep numbers in perspective.
 - Difference between a 5- and 10-year payout to trust translates to 10%-15% difference in value (under most assumptions). Tax priorities can be secondary to client's other planning goals.
- Recognize no effective way around the 10-year rule. SECURE Act will accelerate taxes for most beneficiaries.