

# IRAS IN ESTATE PLANNING

April 2023 Update



A FEW  
THINGS TO  
KEEP IN  
MIND

Income tax deferment

Income tax realization

- Who pays?
- When?

Creditor protection

Practical considerations

- Minority
- Incapacity
- Spendthrift
- Family dynamics



BENEFICIARY  
DESIGNATION  
FORM ISSUES

---

Adding exhibits to  
the form

---

Filing with the  
custodian

---

Absence of a  
completed form



IMPORTANT  
TERMS

Required Beginning Date

Required Minimum  
Distribution

Applicable Distribution  
Period

Designated Beneficiary

Eligible Designated  
Beneficiary



## REQUIRED BEGINNING DATE

For IRA owners, this is April 1<sup>st</sup> of the year after the owner turns 72 (formerly 70 ½).

But, beginning in 2024, this is April 1<sup>st</sup> of the year after the owner turns 73.

And then, beginning in 2033, this is increased to age 75.



## REQUIRED MINIMUM DISTRIBUTION

Distribution that must be taken from an IRA each year based on the Applicable Distribution Period.



## REQUIRED MINIMUM DISTRIBUTION ISSUES

---

The deadline for taking an RMD is December 31<sup>st</sup> (but, for the first year, it's April 1<sup>st</sup> of the following year).

---

An RMD is calculated by dividing the account balance as of December 31<sup>st</sup> of the prior year by the applicable distribution period (the life expectancy of the owner or beneficiary).

---

An RMD for the year of death is required if the owner was in pay status (72/73/75).

---

After the IRA owner's year of death, RMDs apply if the owner was in pay status at the time of death OR the beneficiary qualifies to use a life expectancy for the ADP.

---

Old rule: a 50% penalty applies for failure to take an RMD.

New rule: either: (a) a 25% penalty applies; or (b) a 10% penalty applies if the error is fixed within 2 years.



## APPLICABLE DISTRIBUTION PERIOD

The frequency in which distributions must be taken from an IRA.





## APPLICABLE DISTRIBUTION PERIOD

During life, this is the owner's life expectancy.

Following an owner's death, there are four possibilities:

- The beneficiary's life expectancy
- The remaining theoretical life expectancy of the owner
- 5-year rule
- 10-year rule

Table III  
(Uniform Lifetime)

(For Use by:

- Unmarried Owners,
- Married Owners Whose Spouses Aren't More Than 1
- Married Owners Whose Spouses Aren't the Sole Ben

| Age | Distribution Period |
|-----|---------------------|
| 72  | 27.4                |
| 73  | 26.5                |
| 74  | 25.5                |
| 75  | 24.6                |
| 76  | 23.7                |
| 77  | 22.9                |
| 78  | 22.0                |
| 79  | 21.1                |
| 80  | 20.2                |
| 81  | 19.4                |

## UNIFORM LIFE TABLE

- Recalculated each year
- Reduce-by-one method

A graphic of several green leaves, possibly from a plant, positioned in the bottom left corner of the slide. The leaves are layered and have a soft, glowing appearance.

## DESIGNATED BENEFICIARY

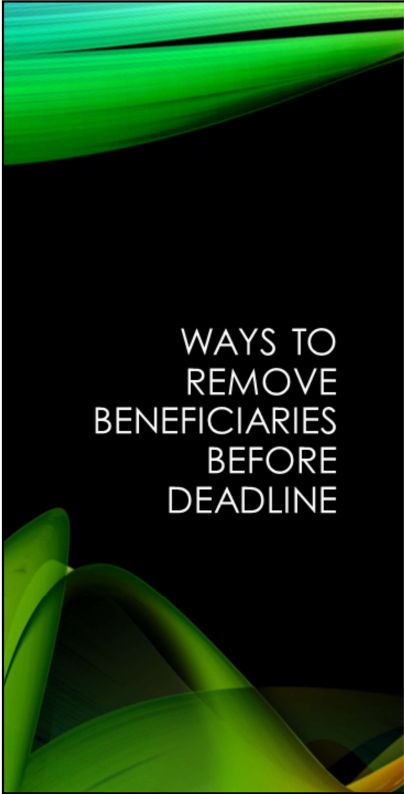
The Designated Beneficiary is "An individual who is designated as a beneficiary under the plan. . . entitled to a portion of an employee's benefit, contingent on the employee's death . . ."

## DESIGNATED BENEFICIARY ISSUES

All must be individuals (except for certain see-through trusts).

Beneficiary does not necessarily have to be named on the beneficiary designation form.

Beneficiaries are fixed as of the date of the owner's death. But, the DB need not be identified until September 30<sup>th</sup> of the year after the owner's death.



WAYS TO  
REMOVE  
BENEFICIARIES  
BEFORE  
DEADLINE

Distribute a beneficiary's share to the beneficiary.

The beneficiary can disclaim.

Divide the account (separate account treatment).



CONSEQUENCE  
OF NO  
DESIGNATED  
BENEFICIARY

If the owner dies before  
RBD -  
5 year rule applies.

If the owner dies after  
RBD -  
use the owner's  
theoretical remaining  
life expectancy.



IF THERE IS A  
DESIGNATED  
BENEFICIARY

---

Distributions taken based  
on the beneficiary's (or  
the owner's) life  
expectancy;

or

---

The 10 year rule applies  
(but how the 10 year rule  
applies depends on  
whether the owner died  
before or after his RBD).



## ELIGIBLE DESIGNATED BENEFICIARY

An Eligible Designated Beneficiary is a Designated Beneficiary who is also one of the following:

- The owner's spouse.
- The owner's minor child.
- A disabled or chronically ill individual.
- An individual who is not more than 10 years younger than the owner.





## 10 YEAR RULE

Applies to a Designated Beneficiary who is not also an EDB.

How it works depends on whether the owner had reached his RBD or not.

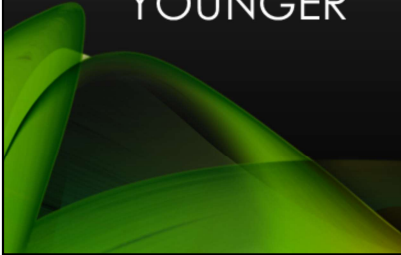
- If not, the account must be distributed in full by December 31<sup>st</sup> of the year containing the 10<sup>th</sup> anniversary of the owner's death.
- If so, annual distributions are required using the beneficiary's life expectancy (single life table, reduce-by-one method) until the year containing the 10<sup>th</sup> anniversary of the owner's death, in which year the balance must be distributed.



## LIFE EXPECTANCY PAYOUT

Different rules apply depending on what kind of an EDB the beneficiary is. The general rules are:

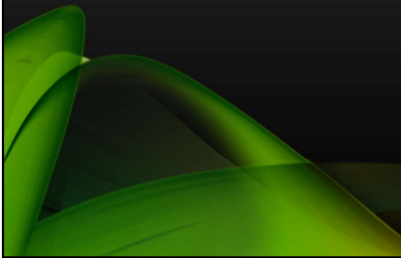
- Each year, starting with the year after the owner's death, the account value as of 12/31 of the prior year, is divided by the remaining life expectancy, as found on the Single Life Table, fixed that year, and then reduced by one, each year thereafter, of the EDB (or of the owner, whichever is longer, if the owner died on or after his RBD).
- The EDB can elect the 10-year rule instead, if the owner died before his RBD.
- But, if the owner died on or after his RBD, 100% of the account must be paid out by the final year of the EDB's life expectancy.



INHERITED IRA  
FOR AN  
INDIVIDUAL  
NOT MORE  
THAN 10  
YEARS  
YOUNGER

The general rules apply.

INHERITED IRA  
FOR A  
DISABLED OR  
CHRONICALLY  
ILL INDIVIDUAL



The general rules apply.



## INHERITED IRA FOR A MINOR CHILD

General rules apply, except, once the child beneficiary reaches age 21 or dies, the 10-year rule kicks in, requiring the account balance to be paid in full before December 31<sup>st</sup> of the year in which the beneficiary reaches age 31 (or the year containing the 10<sup>th</sup> anniversary of death, if shorter).



## SPOUSAL ROLLOVER

A surviving spouse can roll the IRA in to her own IRA, and thus it becomes her own.

- No limits on when this can be done.
- However, if done after the surviving spouse turns 71, the surviving spouse can't roll over the total amount that would have been RMDs if the account was in her name previously.



## INHERITED IRA FOR A SPOUSE

If the surviving spouse does not roll over the account, the general rules apply except:

- The first RMD is due either the year after the owner's death or the year he would have reached age 72/73/75, whichever is later.
- The ADP is the surviving spouse's life expectancy (recalculated each year) (use the Uniform Life Table if the proper election is made) or the owner's life expectancy, if longer if he died after his RBD.



## SEE- THROUGH TRUST

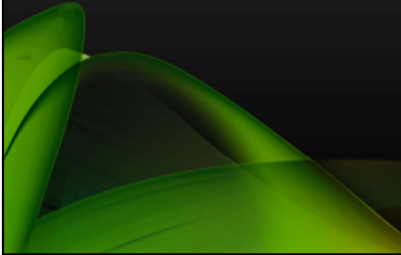
Irrevocable

Valid under state law

Identifiable beneficiaries

Provide documentation to the  
custodian by October 31<sup>st</sup> of  
year following year of death





ADP WHEN  
SEE-  
THROUGH  
TRUST IS  
BENEFICIARY

Look through the trust and use the ADP of the trust's beneficiary:

- If no DB:
  - 5 year rule; or
  - Remaining theoretical life expectancy of the owner.
- If the trust beneficiary is a DB:
  - The beneficiary's life expectancy;
  - The owner's theoretical remaining life expectancy; or
  - 10 year rule.



SO MANY  
QUESTIONS!

If the trust has multiple beneficiaries,  
which beneficiaries count?

What if some are EDBs and some  
are not?

What if the beneficiary is another  
trust?

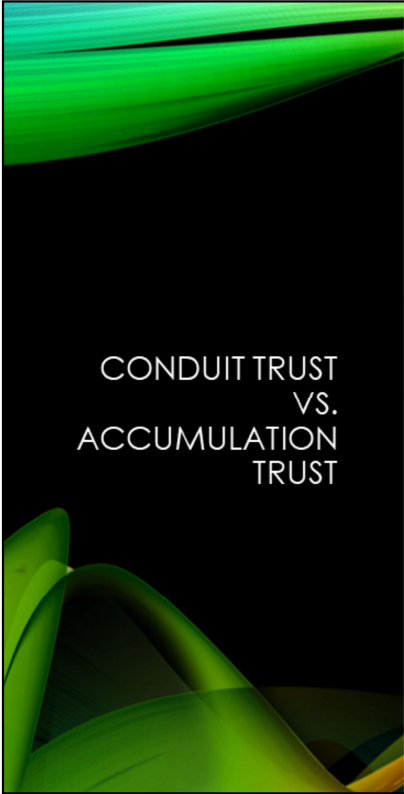
What happens if the trust is modified  
or decanted?

Do we have to structure the trust in  
any particular way for an EDB?



## TRUST BENEFICIARY TIERS

- First Tier—All trust beneficiaries who are eligible to receive benefits as a result of the IRA owner's death. The only death we're waiting for is the owner's death.
- Second Tier—All trust beneficiaries that *could* receive benefits if they are not all distributed to the First Tier beneficiaries. Really, there are two kinds of second tier beneficiaries:
  - Trust beneficiaries who will inherit upon the death of the First Tier beneficiary(ies)
  - Trust beneficiaries who will inherit only if other Second Tier beneficiaries die.



CONDUIT TRUST  
VS.  
ACCUMULATION  
TRUST

Conduit Trust—all withdrawals flow through the trust to or for the beneficiary or beneficiaries.

- Only look at Tier 1 beneficiaries
- No need to count any contingent (Tier 2) beneficiaries.

Accumulation Trust (any trust that is not a conduit trust).

- Count Tier 1 beneficiaries
- And count certain Tier 2 beneficiaries.

## WHOM DO WE REALLY COUNT? MORE RULES

|           |  |
|-----------|--|
| Disregard | Disregard any individual who predeceased the owner and any individual who is not yet born.   |
| Disregard | Disregard beneficiaries removed before the September 30 <sup>th</sup> deadline.  |
| Disregard | Disregard individuals who could become beneficiaries through the exercise of a power of appointment (unless the power is actually exercised).              |
| Disregard | Disregard beneficiaries that take only if a Tier 2 beneficiary dies (and disregard ALL Tier 2 beneficiaries if we're dealing with a conduit trust).        |
| Disregard | Disregard any Tier 2 beneficiaries who take only if the Tier 1 beneficiary dies before age 31 (because the Tier 1 beneficiary will take outright by then). |
| Add       | Add individuals who become beneficiaries before the 9/30 deadline through decanting or reformation.  |



SEPARATE  
ACCOUNT  
TREATMENT?

Separate account treatment is not available unless subtrusts are named on the beneficiary designation form **or** the beneficiaries are disabled or chronically ill.



CHANGES TO  
THE TRUST AFTER  
THE SEPTEMBER  
30<sup>TH</sup> DEADLINE

If the trust is modified or decanted or a power of appointment exercised after September 30<sup>th</sup> of the year following the year of death, the trust is retested. Retesting cannot improve the ADP. But, it can make it worse.



THE  
TRUST IS  
A DB,  
NOW  
WHAT?

Is it an Eligible Designated Beneficiary? If not, the 10 year rule applies:

- If the owner died before his RBD, then 100% must be distributed by 12/31 of the year containing the 10<sup>th</sup> anniversary of the IRA owner's death.
- If the owner died after his RBD, then annual distributions are required, using the life expectancy of the oldest trust beneficiary, through the ninth year, using the reduce by one method and using the single life table. In the last year, the remainder must be withdrawn.





BUT,  
MIGHT  
THE TRUST  
BE AN  
EDB? IF  
SO...

- Do we have a trust for a chronically ill or disabled EDB (even if there are non-DB beneficiaries)? If so, we get EDB treatment, using the life expectancy of the oldest trust beneficiary (generally).
- Do we have a trust for at least one minor child (and no non-DBs)? If so, we get EDB treatment, using the life expectancy of the oldest trust beneficiary (generally).
- Do we have a trust for all EDBs? If so, we get EDB treatment, using the oldest beneficiary's life expectancy (generally).
- Do we have a trust for a spouse and no non-DBs? We get EDB treatment. If a conduit trust is used, we get spousal treatment.

# DRAFTING THE TRUST

Take care to not trap income if lowering income taxes is a priority

Ensure qualification of see-through status

Conduit or accumulation

Avoiding non-DB treatment due to non-human beneficiaries (including creditors)

Don't allow IRAs to satisfy pecuniary charitable gifts

Analyze whether separate trusts or multi-beneficiary trusts should be used

Address the RMD (accumulate or distribute)

Address distributions in excess of the RMD

Consider trust accounting issues

Address what happens if there is a disclaimer

Name sub-trusts on the beneficiary designation form

If needed, comply with marital deduction rules

If needed, comply with SNT rules

Consider how errors on beneficiary designation can be addressed proactively

Is there adequate flexibility to address changes in the law and circumstances?