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IRA Beneficiary Trusts and Post-Death Administration: Strategies and Tools for Implementation

Navigating RMD Issues, Income Tax and Asset Protection Elections, Establishing Sub-Share Trusts, and More

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1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

Today's faculty features:

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Proper Post-Death Administration of an IRA Beneficiary Trust

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Overview

- The steps necessary to establish the sub-share trusts are similar to those establishing sub-share trusts under a Living Trust
- However, there are several critical implementation steps and issues that are unique to the IRA Inheritance Trust® (or most other IRA Beneficiary Trusts)
 - Verifying beneficiaries on IRAs and qualified retirement plans and determining “measuring lives” for required minimum distribution (“RMD”) purposes



Overview

- Unique implementation steps (cont'd)
 - Coordinating with the Trustee of the Trustor's Living Trust and Executor of the Trustor's Estate on numerous estate tax related issues
 - Coordinating with the beneficiaries and their financial advisors on their post-death income tax and asset protection choices and implementing those choices
 - Beneficiary disclaimers
 - Trust Protector actions
 - Properly retitling the IRAs (or qualified retirement plans, called hereafter "QRPs")
 - Coordination with custodians (or plan administrators)



Overview

- Unique implementation steps (cont'd)
 - Properly withdrawing RMDs and then keeping them in trust or paying them to the beneficiaries
 - Meeting specific action time frames established under IRC/Regulations
 - On or before the date 9 months after the Trustor's date of death
 - On or before 9/30 of the year after death ("YAD")
 - On or before 10/31 of the YAD
 - On or before 12/31 of the YAD



Initial Implementation Steps - - On or Before 9 Months After Date of Death

- Install the Trustee
 - Of the master IRA Inheritance Trust®, rather than the individual sub-share trusts
 - Trust Certification
- Communicate with the IRA custodian (or QRP administrator) and determine/verify
 - Primary and secondary beneficiaries recorded on custodian's record
 - Problems may arise if records do not match planning done or known Beneficiary Designation Form ("BDF") filed



Initial Implementation Steps - - On or Before 9 Months After Date of Death

- Communication with IRA Custodian (cont'd)
 - Determine whether individual IRAs (or QRPs) are traditional or Roths
 - Whether the Trustor took RMD for year of death
 - Technically required by 12/31 of the year of death, but IRS typically waives late penalty
 - Should be properly calculated and taken when sub-trusts established (payment does not go to Trustor's estate or Living Trust)



Initial Implementation Steps - - On or Before 9 Months After Date of Death

- Establish communication with beneficiaries
 - Trustee Notice
 - Advise to seek appropriate professional assistance regarding income tax and asset protection choices to be made at time sub-share trust established
 - May offer your services by separate engagement, with Trustee's consent?
 - Opportunity to coordinate with beneficiary's (or Trustee's) CPA, financial advisor, attorney (or make referral to the beneficiary or Trustee)



Initial Implementation Steps - - On or Before 9 Months After Date of Death

- Key decisions to be made by Trustee and/or beneficiaries
 - If surviving spouse is primary IRA beneficiary, will he/she do rollover to own new IRA?
 - Preferable in most cases
 - May then need to do (or amend) own IRA Inheritance Trust® and file appropriate BDF with custodian
 - IRA Inheritance Trust® of deceased Trustor then “dies on the vine”
 - Note: spousal rollover can be done more than 9 months after death



Initial Implementation Steps - - On or Before 9 Months After Date of Death

- Key decisions (cont'd)
 - Will a beneficiary exercise a disclaimer?
 - Surviving spouse may disclaim and IRA passes to IRA Trust (or directly to Exemption and/or Marital sub-trust), if so designated on BDF
 - May want to do to utilize more estate tax exemption (but weigh option of new “portability” election)
 - May want asset protection afforded by Exemption and Marital trusts
 - Required to also disclaim any powers of appointment over Exemption and Marital Trusts



Initial Implementation Steps - - On or Before 9 Months After Date of Death

- Key decisions regarding disclaimers (cont'd)
 - Surviving spouse may thereafter disclaim interest in Exemption and/or Marital Trusts (if they are established)
 - Stretchout, estate tax and asset protection reasons
 - Non-spouse beneficiaries may also disclaim
 - Stretchout, income tax, estate tax and asset protection reasons



Initial Implementation Steps - - On or Before 9 Months After Date of Death

- Key decisions regarding disclaimers (cont'd)
 - Disclaimers must be done timely and in writing
 - Although may have until 9 months after death, should be done much earlier
 - Once disclaimers are made (or beneficiaries have decided not to do), then know “final” beneficiaries of the Trust and can determine type of sub-share trust most appropriate to each
 - Conduit (if adult, capable of handling money and little or no asset protection concerns)
 - Accumulation (lifetime, spendthrift or special needs trust warranted, or asset protection concerns)
 - Depending on trust design, Trust Protector may need to exercise “toggle switch”; this should be done within 9 months of death, though appears not technically required before 9/30 YAD
 - May be other ways to reform trust



Initial Implementation Steps - - On or Before 9 Months After Date of Death

- Key decisions (cont'd)
 - Will the Trust Protector need to come in and act?
 - If so, the Trust Protector must be installed
 - First Successor Trustee who is independent (within meaning of IRC 674(c)) acts as “Special Co-Trustee”
 - Special Co-Trustee appoints Trust Protector
 - Attorney may act only as temporary Trust Protector (not preferred, but may need to if time running short)



Initial Implementation Steps - - On or Before 9 Months After Date of Death

- Key decisions regarding Trust Protector (cont'd)
 - If sub-share trust is converted from conduit to accumulation, special other steps may need to take place to maximize RMD stretchout
 - Limit future beneficiaries under beneficiary's limited power of appointment and contingent beneficiary paragraph of trust
 - Renounce Trust Protector power to again exercise toggle switch



Initial Implementation Steps - - On or Before 9 Months After Date of Death

- Key decisions (cont'd)
 - Should each beneficiary do some additional estate planning?
 - Name successor Trustees of their individual sub-share trust
 - Exercise any limited power of appointment
 - Coordinate these with own Living Trust/estate plan



Initial Implementation Steps - - On or Before 9 Months After Date of Death

- Coordination with the Trustee/Executor of Decedent's Living Trust/Estate
 - Should a 706 be filed to elect portability?
 - If a 706 will be filed (or extended) and a tax payment will be due, how will estate taxes be allocated?
 - May be an issue if the beneficiaries of the IRA Trust (or their %s) are different than under the Living Trust
 - Must refer to specific tax allocation paragraphs of each trust
 - Consider also possible right of Estate to seek reimbursement under IRC 2207A



Initial Implementation Steps - - On or Before 9 Months After Date of Death

- Coordination with Trustor/Executor (cont'd)
 - If Exemption Trust or IRA Trust is to be set up, Living Trust should be given first priority in utilizing exemption amount (or Executor given first choice to utilize “portability”)
 - May depend upon respective document terms
 - Same issue regarding allocation of generation skipping transfer tax (“GST”) exemption amount (normally don’t prefer to use GST exemption for IRAs because RMDs make them wasting assets)



Further Implementation Steps - - On or Before 9/30 YAD

- Payment of the Decedent's (or his/her estate's) debts, taxes and expenses
 - The preference is not to pay these from the IRA Trust, but this could become necessary if decedent's Living Trust and estate lack cash or the ability to raise cash by sales of assets or loans
 - The Trustee should be directed to seek loans from the IRA Trust beneficiaries before paying these items from trust assets



Further Implementation Steps - - On or Before 9/30 YAD

- Payment of debts, taxes, expenses (cont'd)
 - If these will be paid from the IRA Trust, they should be paid on or before 9/30 or stretchout of RMDs may jeopardized
 - Trust provisions may so require payout by this date



Further Implementation Steps - - On or Before 9/30 YAD

- “Measuring lives” for RMD stretchout must be finally determined
 - Who is left after disclaimers?
 - Who is left after possible payouts by Trustee to eliminate “bad” beneficiaries, such as older individuals or charities?
 - Death of a beneficiary between Trustor’s death and 9/30 YAD irrelevant for RMD purposes but may affect establishment of sub-share trusts
 - Which beneficiaries are “counted”?
 - Conduit trust
 - Accumulation trust



Further Implementation Steps - - On or Before 9/30 YAD

- Sub-share trusts established
 - Usually same sub-share setup procedures as with a Living Trust
 - Sub-share trust named
 - Should include name of beneficiary, for custodian RMD reasons
 - Trustee of particular sub-share trust installed
 - If a young beneficiary is sole Trustee or asset protection concerns, trust document may permit Trustee, beneficiary, or Trust Protector to bring in independent bank or trust company as a Co-Trustee



Further Implementation Steps - - On or Before 9/30 YAD

- Sub-share establishment and procedures (cont'd)
 - File for EIN
 - Income tax returns will be due for trust sub-share
 - Conduit trust will result in any tax being paid at beneficiary's rate, so long as distribution made from Trust within 65 days of end of calendar year when RMD received by trust
 - In some cases, more than one sub-share trust may be established for a beneficiary
 - Such as to allocate GST exemption
 - Also, if some Roth IRAs, for practical reasons may want them payable to one sub-share trust and the traditional IRAs to another



Further Implementation Steps - - On or Before 9/30 YAD

- Sub-share trusts established (cont'd)
 - Transferring assets to sub-share trusts is different with IRAs and QRPs
 - Not transferred into name of the sub-share trust
 - “Retitled” with the custodian, keeping the original owner’s name on it
 - “(Decedent’s name) IRA FBO (Name of beneficiary's sub-share trust)”
 - If a QRP, the Trustee must establish new “Inherited IRA” as above and have administrator transfer funds directly to it
 - If a QRP and was not already a Roth, the Inherited IRA may be designated from the start as a Roth (but must consider income tax consequences first)



Further Implementation Steps - - On or Before 9/30 YAD

- Sub-share establishment and transfers (cont'd)
 - If IRA will go to more than one beneficiary sub-share trust, custodian should split the IRA first
 - Each individual new IRA retitled as above
 - Must be prorata division of assets between the new IRAs
 - Note: while it is not technically required that establishment and funding of the sub-share trusts be finalized by 9/30 YAD, this is the conservative reading of the Regulations by many commentators



Further Implementation Steps - - On or Before 10/31 YAD

- Copy of IRA Trust to the custodian (or plan administrator)
 - Or summary of its beneficiary provisions, per the Regulations
- Don't bother sending while Trustor alive!
- Should be done when IRA custodian first contacted
 - More conservative approach, so don't miss deadline
 - However, if all beneficiaries not yet settled (disclaimers or Trust Protector powers may be exercised), could confuse custodian and result in paperwork being processed that could later be difficult to reverse and may jeopardize stretchout



Further Implementation Steps - - On or Before 12/31 YAD

- First annual RMDs must be paid out
 - IRA withdrawals made by Trustee, payable to the Trust
 - Deposited into a trust account
 - If conduit trust, same amount then paid out to beneficiary
 - Preferably on or before 12/31 YAD (or same calendar year as IRA withdrawal)
 - In any event, should be done no later than 65 days after the end of the calendar year



Further Implementation Steps - - On or Before 12/31 YAD

- Payment of first annual RMD if conduit (cont'd)
 - Note: the Trustee may deduct, before paying out to beneficiary, normal/regular trust administration expense (such as Trustee or custodian fees, tax return prep fees)
 - If beneficiary is a minor, an UTMA account should be established (with Trustee or guardian as custodian) and payment made from the trust to this account
- Later years' RMDs done in same manner
- Final distribution of a sub-share trust
 - IRA "retitled" FBO individual name of beneficiary (decedent's name still remains on it, so not a taxable event)



Troubleshooting Problems

- Problems could arise with BDF, terms of the Trust, or missed deadlines
- Trustee may seek Court help
 - Trust reformation
 - May or may not be accepted by IRS, depending on facts
 - Reformation of BDF
 - Not likely to be accepted by IRS
 - Better approach may be to do “informally” with the custodian, if possible



Troubleshooting Problems

- Trustee may seek modification of the Trust by agreement with the beneficiaries
 - Depends upon state law
 - IRS may or may not accept, depending on facts
- The IRA Trust provisions may give the Trustee and/or Trust Protector the power to amend or terminate a sub-share trust, in order to qualify for maximum RMD stretchout
- Alternatively, or in conjunction with any of the above troubleshooting options, an IRS Private Letter Ruling may be sought



Troubleshooting Problems

- Can't get the custodian to cooperate
 - Provide a “hold harmless” agreement signed by Trustee and beneficiaries
 - The “Nuclear” Bomb



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Any Questions?

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