Estate Administration for IRAs and Qualified Plans

– After the SECURE Act

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SECURE ACT
THE “TEN-YEAR RULE”

EFFECTIVE DATE
January 1, 2020
SECURE ACT
TEN-YEAR RULE

Modification of
Required Minimum Distribution Rules
for Designated Beneficiaries

Basically, requires all IRAs and Qualified Plans to be distributed within 10-years of death
SECURE ACT
TEN-YEAR RULE

• Exceptions for certain beneficiaries (“eligible designated beneficiary”)
  – Surviving Spouse
  – The employee’s Children under the age of majority (not grandchildren or any other children)
  – Disabled
  – Chronically ill
  – Individual not more than ten years younger than employee

IRC § 401(a)(9)(E)(ii)
Foundation Concepts
Introduction to Retirement Distribution Planning

Foundation Tax Concepts

- IRAs are not taxed until distributed
- Distributions must begin no later than one’s Required Beginning Date (RBD)
- IRA elections are required after death
- Deaths on or Before December 31, 2019 – Life Expectancy Rules
- Deaths on or After January 1, 2020 – 10-Year Rule Generally
- Roth IRAs Require Special Planning
- Basis Requires Special Planning
- NUA Requires Special Planning
Foundation Property Law Concepts

• Wills control probate assets
• Trusts control trust assets
• IRAs and qualified retirement plans are controlled by beneficiary designation form or default provisions of contract
Foundation Concepts

- IRC Sec. 408(g)
- IRA rules are applied without regard to any community property laws
  - In *Morris*, the Court held that express statutory provisions of IRC §408(d) and §408(g) overrode state law. TC Memo 2002-17
- Distribution taxable to IRA owner rather than ½ to wife in community property situation
Retirement Equity Act of 1984 (REA)

• 26 USCA Sec. 417 (1984)
• ERISA covered plans
  – IRAs not covered
    » IRA custodians, however, may require their own consent when someone other than spouse is named as beneficiary
• Plans must comply with the requirements of IRC Sections 401(a)(11) and 417 in order to remain qualified
Retirement Equity Act of 1984 (REA)

• Treas. Reg Sec. 1.401(a)-20
• Must provide both a qualified joint and survivor annuity (QJSA) and a qualified preretirement survivor annuity (QPSA) to remain qualified
• Spousal consent required to waive the QJSA or the QPSA
• Cannot be waived in prenuptial agreement because it is before marriage
• If spouse is legally incompetent to give consent, the spouse's legal guardian, even if the guardian is the participant, may give consent
PROPERTY LAW RIGHTS AT DEATH
ERISA Plans

Who Dies First?

Participant

Is the spouse the 100% beneficiary?

Yes

To Spouse

No

REA Waiver Requirements Met?

Yes

To Named Beneficiary

No

Spouse

STOP
Spouse’s property law rights terminate at death

All to Spouse
Stretch Out IRAs Under 2019 Law

TRADITIONAL IRA DISTRIBUTION FLOWCHART

Is the IRA owner living?

Yes

Is the spouse the “sole beneficiary”? Yes

Is the spouse more than 10 years younger than IRA participant? Yes

Calculate using Joint and Last Survivor Table

No

Calculate using Uniform Lifetime Table

No

Calculate using Uniform Lifetime Table

Spouse

Trust

Trust by disclaimer

Charity

Estate

Children or grandchildren by disclaimer

Children or grandchildren

Yes

Did owner die before RBD?

Yes

Did you create separate accounts by Dec. 31st of year following the year of death?

No

Five-Year Rule

Remaining life expectancy of decedent as of death based on Single Life Table

Inherited IRA

Were separate shares created by Dec. 31st of year following the year of death?

Yes

Life expectancy of oldest beneficiary

No

OR the owner’s life expectancy if the owner is younger than the oldest trust beneficiary

Rollover (take RMD, if applicable, then go to step one treating survivor as new owner)

Rollover or Inherited IRA

Please email us for more information on this chart and for other education products: contactus@keeblerandassociates.com

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Stretch Out IRAs

“Inherited” IRA – Key Terms

- **Required Beginning Date (RBD)** – the date when distributions are required to begin
- **Required Minimum Distributions (RMD)** – the minimum amount that must be distributed from the account each year
- **Beneficiary** – person/persons/entity named as beneficiary of the account
- **Designated Beneficiary** – person or trust that qualifies as a designated beneficiary under the 401(a)(9) Regulations. A qualified designated beneficiary is allowed to utilize the life expectancy of a beneficiary. Term defined in Treas. Reg. Sec. §1.401(a)(9)-4, Q&A 1.
Stretch Out IRAs (Pre-Secure)

“Inherited” IRA

- An IRA is treated as “inherited” if the individual for whose benefit the IRA is maintained acquired the IRA on account of the death of the original owner.
- Under 2019 law, the IRA assets could be distributed based upon the life expectancy of the beneficiary.
- Some of these concepts continue to apply under Secure.

IRC Sec. 401(a)(9)
Stretch Out IRAs

• Two Strategies
  – Spousal Rollover
  – Inherited IRA

• Advantages
  – Rollover delays RMD until spouse’s own RBD
  – Inherited IRA provisions allow beneficiary’s life expectancy to be used for distributions after death of IRA owner.

Available before and after Secure
Stretch Out IRAs

“Inherited” IRA – Spousal Beneficiary – Rollover

- Exception to Inherited IRA rules.
- Only available to surviving spouse.
- Allows spouse to rollover assets received as beneficiary to a new IRA in his/her own name.
- Spouse’s age used to determine when required minimum distributions must begin.
- Spouse may use the Uniform Lifetime Table to determine distributions.
- Both plans, Traditional IRAs and Roth IRAs may be rolled over.
Stretch Out IRAs

*Income in Respect of a Decedent (IRD)*

- **Income in respect of a decedent (IRD)** – is all items of gross income in respect of a decedent which were not properly included as taxable income in a tax period falling on or before a taxpayer’s death and are payable to his/her estate and/or another beneficiary
- IRAs & Qualified Plans will generate IRD
- Potential 691(c) Deduction

IRC Sec. 691(a)
401(a)(9) Regulations

Foundational Concepts

Required Minimum Distribution (RMD)

• RMDs are calculated based upon the aggregate prior year ending account balance divided by the applicable life expectancy factor

\[
\text{RMD} = \frac{\text{Prior Year 12/31 Balance}}{\text{Life Expectancy Factor}}
\]
401(a)(9) Regulations

Foundational Concepts

• Post-Mortem Distribution Amounts
  – Uniform Lifetime Table
  – Single Life Table
  – Joint and Last Survivor Table
    • Available where the spouse is the sole beneficiary and is more than 10 years younger than the account owner
  – Five-Year Rule

New in the SECURE ACT
New Ten-Year Rule
Eligible Designated Beneficiaries
401(a)(9) Regulations

Foundational Concepts

- Post-death RMDs based on whether “designated beneficiary” exists
- Qualifying “designated beneficiaries”
  - Individuals
  - Certain Trusts
- Non-qualifying “Non-designated beneficiaries”
  - Estates, Charities, Most Trusts
- Eligible Designated Beneficiaries
401(a)(9) Regulations

Foundational Concepts – Pre-SECURE Law

• Death before age 70½ (changed to age 72 by the Secure Act)
  – Life expectancy distributions if you have a designated beneficiary
  – If no designated beneficiary, five-year rule
  – Distributions must begin by December 31st of the year after death
    » Failure to do so does not automatically cause the five-year rule to apply
    » Delayed distributions – spousal beneficiary

• Death after age 70½ (changed to age 72 by the Secure Act)
  – Life expectancy distributions if you have a designated beneficiary
  – If no designated beneficiary, ghost life expectancy rule
  – Distributions must begin by December 31st of the year after death
  – Year of death distribution – life expectancy of IRA owner
### 401(a)(9) Regulations

#### Foundational Concepts – Pre-SECURE Law

<table>
<thead>
<tr>
<th></th>
<th>Death Before Required Beginning Date</th>
<th>Death On or After Required Beginning Date</th>
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</thead>
<tbody>
<tr>
<td>Designated</td>
<td><strong>Life Expectancy Rule</strong></td>
<td><strong>Life Expectancy Rule</strong></td>
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<tr>
<td>Beneficiary</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-Designated</td>
<td><strong>Five-Year Rule</strong></td>
<td><strong>Owner’s “Ghost” Life Expectancy Rule</strong></td>
</tr>
<tr>
<td>Beneficiary</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Both the Five-Year and “Ghost” Life Expectancy appear to have survived the Secure ACT for non-designated beneficiaries.
<table>
<thead>
<tr>
<th>Eligible Designated Beneficiary</th>
<th>Death Before Required Beginning Date</th>
<th>Death On or After Required Beginning Date</th>
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<tbody>
<tr>
<td>Life Expectancy Rule</td>
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<tr>
<td>Designated Beneficiary</td>
<td>10-Year Rule</td>
<td>10-Year Rule</td>
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<td>Non-Designated Beneficiary</td>
<td>Five-Year Rule</td>
<td>Owner’s “Ghost” Life Expectancy Rule</td>
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</tbody>
</table>
401(a)(9) Regulations

Foundational Concepts – Pre-SECURE Law

• Generally, if individual beneficiaries exist, post-death RMDs are based upon oldest designated beneficiary’s life expectancy under the Single Life Table

• If separate shares are created by 12/31 of the year following the year of death, then each beneficiary’s life expectancy is used
A designated beneficiary determines his/her RMD life expectancy factor by referencing the Single Life Table.

The individual beneficiary calculates the RMD for the first year (i.e. the year following the year of the IRA owner’s death) by dividing the IRA balance by the RMD factor.

Each year thereafter, the designated beneficiary calculates the RMD by subtracting one from the RMD factor.

- The “subtract one” method.
401(a)(9) Regulations

Foundational Concepts – Pre-SECURE Law

• Example
  – Agnes died in 2019, naming her granddaughter, Iris, as the beneficiary of her IRA. Assuming that Iris will be 23 in 2020, Iris’s RMD factor for 2020 would be 60.1.
  – Beginning in 2020 and every year thereafter, Iris’s RMD factor will be reduced by one (i.e. 2020 = 59.1, 2021 = 58.1, etc.).
401(a)(9) Regulations

*Foundational Concepts – Critical dates*

- **September 30** of the year following the year of death
  - Date at which the beneficiaries are identified
- **October 31** of the year following the year of death
  - Date at which trust documentation (in the case where a trust is named as a designated beneficiary) must be provided to the custodian
- **December 31** of the year following the year of death
  - Date at which the first distribution must be made by each IRA beneficiary
  - Date at which separate shares must be created
401(a)(9) Regulations

Foundational Concepts

September 30th Determination Date

- “Designated beneficiary” is not determined until September 30th of the year following the year of the IRA owner’s death
  - Treas. Reg. § 1.401(a)(9)-4, Q&A 4(a)
  - Allows for disclaimer planning

- If a beneficiary dies before the September 30th date without disclaiming, such beneficiary continues to be treated as a beneficiary in determining the designated beneficiary
  - Treas. Reg. § 1.401(a)(9)-4, Q&A 4(c)
Example #1

- Jane names a trust as beneficiary of her IRA. 90% of the trust is payable to her children over their lifetimes. 10% of the trust is payable to Jane’s favorite charity.
- If the charity’s 10% is paid out of the trust by September 30th of the year following the year of Jane’s death, the charity’s interest will not taint the rest of the trust.
401(a)(9) Regulations

Foundational Concepts

September 30th Determination Date

• Example #2
  – John names his sister as primary beneficiary of his IRA and his nephew as contingent beneficiary.
  – If John’s sister dies before September 30th of the year following the year of John’s death without performing a qualified disclaimer, RMDs are still calculated based on the sister’s life expectancy.
401(a)(9) Regulations

Foundational Concepts

September 30th Determination Date

• Example #3
  − John names his wife as primary beneficiary of his IRA and his grandchild as contingent beneficiary.
  − If John’s wife performs a qualified disclaimer by September 30th of the year following the year of John’s death, RMDs can be calculated based on the grandchild’s life expectancy.
Disclaimer Planning

- 2019 Deaths
- 2020 Deaths
Disclaimer Planning

**Overview**

- Disclaimer must be “qualified”
  - In writing
  - Within nine months
  - No acceptance of the interest or any of its benefits
  - Interest passes without any direction on the part of the person making the disclaimer
- A disclaimer of plan benefits or IRA is neither a prohibited assignment or alienation

IRC § 2518; GCM 39858
Disclaimer Planning

• Example
  – Alex dies at age 70. Alex’s wife disclaims amount of Alex’s unified credit to bypass trust for benefit of herself and their children
    – Disclaimer must occur within nine months from date of death
    – Disclaimer must be served to the IRA custodian
    – Disclaimer must be fractional to avoid immediate income taxation
Disclaimer Planning

Revenue Ruling 2005-36

• A beneficiary's disclaimer of a beneficial interest in a decedent's IRA is a qualified disclaimer even though, prior to making the disclaimer, the beneficiary receives the required minimum distribution for the year of the decedent's death from the IRA.
Disclaimer Planning

Post-Secure Ideas

• A Designated Beneficiary (10-year Rule Beneficiary) may be able to disclaim to:
  – An Exempted Designated Beneficiary, capturing a period of life expectancy distributions
  – A Non-Designated Beneficiary, capturing “Ghost” life expectancy distributions
  – A Designated Beneficiary subject to lower income tax rates
Spousal Rollover From Estates and Trusts
Spousal Rollover

Spousal Rollover Planning Through Estate

IRA → Estate → Spouse sole residuary beneficiary

Surviving spouse is executor

PLR 201618011
Spousal Rollover

Spousal Rollover Planning Through Trust

IRA → Rev. Trust

Marital Trust GPA

Spouse is trustee vested with power to allocate assets among trusts

Credit Shelter Trust

Spouse Trustee of GPA Trust

See PLR 201225020 Rollover Allowed
Spousal Rollover

Spousal Rollover Planning Through Trust

IRA → Estate of IRA owner → Pour over will → Revocable Trust → All to spouse unless disclaimed

Surviving spouse is sole executor

Spouse is sole trustee
Spousal Rollover

Spousal Rollover Trap

• **Spousal rollover before age 59½**
  – Will cause pre-59½ distributions to be subject to the 10% early distribution penalty
    » See *Sears v. Commissioner*, TC Memo 2010-146
  – If no rollover occurred, pre-59½ distributions can be taken penalty free

• **Solution**
  – Do not perform spousal rollover until spouse reaches age 59½
THE NEW SPOUSAL ROLLOVER TRAP

• Prior to SECURE Act, a spousal rollover was generally the best practice to preserve the IRA

• However, for many it may now be better to begin distributing the IRA earlier in order to minimize exposure to higher tax brackets
THE NEW SPOUSAL ROLLOVER TRAP

Old Best Practice

Spousal Rollover

“Inherited” IRA

Deceased Spouse

Surviving Spouse

Children
THE NEW SPOUSAL ROLLOVER TRAP

Old Best Practice & the New Spousal Rollover Trap

First Death

8 Years ?

Second Death

10 Years

Lifetime RMDs

Ten-Year Rule Distributions
THE NEW SPOUSAL ROLLOVER TRAP

New Best Practice

Deceased Spouse

Spousal Rollover

“Inherited” IRA

Surviving Spouse

“Inherited” IRA

Children
THE NEW SPOUSAL ROLLOVER TRAP

New Best Practice

Roth Conversions or Distributions

Ten-Year Rule Distributions

Lifetime RMDs

First Death

8 Years ?

Second Death

10 Years
Charitable Planning with IRAs
Charitable Planning with IRAs

Basic Overview

• Available Options to Transfer IRD Assets of Charity
  – Name the charity as the designated beneficiary of the assets
  – Specific Bequest of IRD assets to charity under a will
  – Power of Executor to make a non-pro rata distribution to Residuary Beneficiaries
  – Assignment of IRD to charity to satisfy a Pecuniary Bequest
  – Recognition of income with § 642(c) charitable deduction
  – Recognition of income without a § 642(c) charitable deduction
Charitable Planning with IRAs

Basic Overview

§ 642(c)(1) General rule

In the case of an estate or trust, there shall be allowed as a deduction in computing its taxable income any amount of the gross income, without limitation, which pursuant to the terms of the governing instrument is, during the taxable year, paid for a purpose specified in section 170(c)
Charitable Planning with IRAs

Basic Overview

§ 642(c)(2) Amounts permanently set aside

There shall also be allowed as a deduction in computing its taxable income any amount of the gross income, without limitation, which pursuant to the terms of the governing instrument is, during the taxable year, permanently set aside for a purpose specified in section 170(c).

*Applies only to estates – not to trusts funded later than 1969

See the remainder of the statute for details.
Managing the Income Tax
Consequences of the Ten-Year Rule

SOLUTIONS TO ANALYZE
Solutions – Key Concepts

- Retain Income Tax Deferral
- Bracket Management within a Family
- Fulfill Charitable Goals with IRD
- Manage State Income Taxes
- Fiscal Year Planning

The professional’s expertise must include an understanding of Fiduciary Accounting & Income Taxation
2020 Ordinary Income Tax Rates

**Single**
- $<9,875: 10%
- $40,125: 12%
- $85,525: 22%
- $163,300: 24%
- $207,350: 32%
- $518,400+: 35%
- $622,050+: 37%

**MFJ**
- $<19,750: 10%
- $80,250: 12%
- $171,050: 22%
- $326,600: 24%
- $414,700: 32%
- $622,050+: 35%

**199A Threshold**
- $40,125
- $85,525
- $163,300
- $207,350
- $518,400+

**NIIT Threshold**
- $<9,875
- $40,125
- $85,525
- $207,350
- $518,400+
Foundational Concepts

General Fiduciary Tax Concepts

• Income taxed to either the estate/trust or the beneficiaries
  – If income is accumulated, then the income is taxed to the trust/estate
  – If income is distributed, then the trust/estate gets an income tax deduction and beneficiaries report taxable income

IRC §§ 661-663
Foundational Concepts

2020 Ordinary Income Tax Rates for Estates & Trusts

- 37% on income over $12,950
- 35% on income over $9,450 and up to $12,950
- 24% on income over $2,600 and up to $9,450
- 10% on income up to $2,600
Foundational Concepts

Types of “Income”

• Fiduciary accounting income
  – Governed by state law and the trust instrument
  – Determines the amount that may or must pass to the trust’s or estate’s beneficiaries

• Tax accounting income
  – Governed by the federal income tax law
  – Determines who is taxed on the income
Foundational Concepts

Typical Types of “Income” Under Traditional Fiduciary Accounting

• Interest
  – Taxable
  – Tax-exempt

• Dividends

• A portion of IRAs and/or RMDs (varies by state law)
  – RMD rule
  – 10% rule
  – 4% rule
Foundational Concepts

Typical Types of “Principal” Under Traditional Fiduciary Accounting

- A portion of IRAs and/or RMDs (varies by state law)
- Increases in asset value (i.e. growth)
- Realized long-term capital gain
- Realized short-term capital gain
Foundational Concepts

Distributable Net Income (DNI)

• Determines the amount of the trust’s or estate’s income distribution deduction.
• Determines how much the beneficiaries must report as income on their tax returns.
• Determines the character (e.g. interest, dividends, IRAs etc.) of the taxable income in beneficiaries’ hands.

IRC §§ 661-663
Foundational Concepts

Distributable Net Income (DNI)

Trust/Estate
DNI acts as a ceiling for purposes of the allowable deduction

Beneficiary
DNI acts as a ceiling for the total amount of income the beneficiary must report on his/her tax return
Distributable Net Income (DNI)

Example

Assume that a complex trust had the following sources of income and deductions during the current tax year:

- Interest income: $1,000
- Dividend income: $1,000
- IRA distributions: $48,000
- Attorney/accountant fees: $500
## Foundational Concepts

### Distributable Net Income (DNI) Example (cont.)

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
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<tbody>
<tr>
<td>Interest income</td>
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<tr>
<td>Dividend income</td>
<td>1,000</td>
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<tr>
<td>IRA Distributions</td>
<td>48,000</td>
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<td><strong>Total Income</strong></td>
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<td>Less: Attorney/accountant fees</td>
<td>-(500)</td>
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<tr>
<td><strong>Adjusted Gross Income (AGI)</strong></td>
<td><strong>$49,500</strong></td>
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<tr>
<td>Less: Exemption</td>
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<td><strong>Taxable Income</strong></td>
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<td>Taxable Income</td>
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<tr>
<td>Add-In: Exemption</td>
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<tr>
<td><strong>Distributable Net Income (DNI)</strong></td>
<td><strong>$49,500</strong></td>
</tr>
</tbody>
</table>
Foundational Concepts

“65-Day” Rule – IRC 663(b)

• Applies to estates and complex trusts
• Allows fiduciary to treat distributions made within 65 days after year-end to be treated as if they were made as of December 31\textsuperscript{st} of the prior year
  – Limited to DNI (reduced by distributions made during the prior year)
• Election must be made by the due date of the tax return
  – Election is irrevocable
  – Annual election
Foundational Concepts

“65-Day” Rule – IRC Section 663(b)

Distributions made during this period will be treated as have been made as of 12/31/2020 (if a timely election is made)
FISCAL YEAR PLANNING
FISCAL YEAR PLANNING

• An estate (and/or “filing trust” under an IRC §645 election) may opt for a fiscal year-end not to exceed 12 months.
  – A “filing trust” is the decedent’s Qualified Revocable Trust (QRT) prior to death.
  – A probate estate does not need to exist in order to make an IRC §645 election. Instead, the “filing trust” becomes the estate for income tax purposes.
  – The IRC §645 election (using IRS Form 8855) must be made by the due date (including extensions) for the first income tax return.
FISCAL YEAR PLANNING

- By electing a fiscal year for the estate/QRT, the five-year IRA distribution period is allocated over six tax years.

<table>
<thead>
<tr>
<th>Fiscal Year 1</th>
<th>Fiscal Year 2</th>
<th>Fiscal Year 3</th>
<th>Fiscal Year 4</th>
<th>Fiscal Year 5</th>
<th>Fiscal Year 6</th>
</tr>
</thead>
</table>

2019 Tax Year 2020 Tax Year 2021 Tax Year 2022 Tax Year 2023 Tax Year 2024 Tax Year

NOTE: In order for the six-year IRA distribution strategy to work, the first fiscal year must end before December 31st of the year of death (e.g. November 30th)
FISCAL YEAR PLANNING

- Example

<table>
<thead>
<tr>
<th>IRA Distributions (Assuming $1,000,000 IRA at Death)</th>
<th>Normal Fiscal Year</th>
<th>Six-Year Strategy</th>
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<tbody>
<tr>
<td>2019 Tax Year</td>
<td>$200,000</td>
<td>$166,667</td>
</tr>
<tr>
<td>2020 Tax Year</td>
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<tr>
<td>2021 Tax Year</td>
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<td>2022 Tax Year</td>
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<td>2023 Tax Year</td>
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<tr>
<td>2024 Tax Year</td>
<td>$0</td>
<td>$166,667</td>
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<tr>
<td>TOTAL*</td>
<td>$1,000,000</td>
<td>$1,000,000</td>
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</tbody>
</table>

* Assumes 0% growth of the IRA
FISCAL YEAR PLANNING

• Planning considerations
  – An IRC §645 is only valid for the later of: (a) two years from the date of the decedent’s death or (b) six months after the “final determination of estate tax” (if an IRS Form 706 was filed).
  – If an estate is open for more than two years, then an explanation must be made on the IRS Form 1041 as to why the estate is being held open (see IRS Form 1041, Page 2, Other Information, Question 8).
FISCAL YEAR PLANNING

• By having an estate paid to multiple trusts, IRA distributions would be allocated over a great number of distributees, thus lowering overall taxable income.

**OPTION 1 – Outright to Beneficiaries**

$1,000,000 IRA

$200,000/year over five years

Estate

$50,000 $50,000 $50,000 $50,000

B1 B2 B3 B4

**OPTION 2 – Paid in Trust**

$1,000,000 IRA

$200,000/year over five years

Estate

$50,000 $50,000 $50,000 $50,000

T1 T2 T3 T4

$37,500 $37,500 $37,500 $37,500

B1 B2 B3 B4
Estate Administration for Roth IRAs after the SECURE Act
The “Basics” of Roth IRA Estate Administration

General Concepts

• 100% of growth is tax-exempt
• No required minimum distributions at age 72
  — NOTE: Distributions from Roth IRAs cannot be used to fulfill the RMD from a traditional IRA
• RMDs on Inherited Roth IRAs
  • 10 Years for Designated Beneficiaries
  • 10 Years for Designated Beneficiary Trusts
  • Special Rules for Eligible Designated Beneficiaries
  • Special Rules for Certain Eligible Designated Beneficiary Trusts
  • Special Rules for Conduit Trusts
  • Five-Year Rule for Non-Designated Beneficiary Trusts and Estates
Roth Conversions of Inherited Accounts

• Inherited IRA
  – Spouse Beneficiary
    » Can convert inherited traditional IRA to inherited Roth IRA
    » Can perform spousal rollover to Roth IRA
  – Non-Spouse Beneficiary
    » Cannot convert inherited traditional IRA to inherited Roth IRA
    » Can convert inherited qualified plan to inherited Roth IRA (see Notice 2008-30)
Excess Accumulation Penalty
Excess Accumulation Penalty

- A 50% penalty is assessed to the extent that a taxpayer has not taken his/her RMD for the tax year

- **Example**
  - Assume Peter was required to take out $30,000 from his inherited IRA in 2021, but only withdrew $20,000. In this case, Peter would be subject to a $5,000 \[\text{($30,000 - $20,000) x 50\%}\] excess accumulations penalty. Further, Peter would still be required to withdraw the $10,000 deficiency from his inherited IRA.

Review prior year income tax returns for RMD issues
Excess Accumulation Penalty

• If decedent was past his RBD, ensure that RMD for year of death was/is taken by end of that year
  – Payable to beneficiary
  – Request waiver if not timely taken

• RMDs required for Roth IRAs inherited by non-spouse
Excess Accumulation Penalty
Requesting a Waiver

- Under IRC §4974(d), the tax may be waived if the taxpayers can establish that the shortfall in distributions was due to reasonable error and reasonable steps are being taken to remedy the shortfall. An accumulation occurs because of “reasonable error" when it occurs through no fault of the plan participant.
- Complete Form 5329
- Attach letter requesting waiver
- Protecting the executor
Stretch Out IRAs – In Depth
Stretch Out IRAs

“Inherited” IRA

**Old Law Objective**: Prolong IRA and Roth payments over the longest possible period of time (including Life Expectancy), thus increasing wealth to future generations

**New Law Objective**: Prolong IRA and Roth payments over the longest possible period of time (including Life Expectancy), thus increasing wealth to future generations

- Generally only 5 Years for Non-Designated Beneficiaries
- Generally only 10 Years for Designated Beneficiaries
- Special Rules for Eligible Designated Beneficiaries
- Special Rules for Conduit Trusts
Secure Act - Overview

• Changes to Post-Death Distributions
  – Non-Designated Beneficiaries
    • Five-Year Rule
    • “Ghost” Rule
    • Guidance Needed from IRS or Treasury
  – Designated Beneficiaries
    • Ten-Year Rule
  – Eligible Designated Beneficiaries
    • Spouses – Life Expectancy
    • Minor Children – Life Expectancy (modified)
    • Disabled Beneficiaries – Life Expectancy
    • Chronically ill Beneficiaries – Life Expectancy
    • Person within Ten Years of the IRA Owner’s Age – Life Expectancy
Secure Act-Overview
Eligible Designated Beneficiaries

• Minor Child
  – As described in IRC §409(a)(9)(F), a child may be treated as having not reached majority if they have not completed a “specified course of education” and is under the age of 26.
  – If both of the requirements are met, the minor child beneficiary may use the Life Expectancy until 26 years of age.
Secure Act-Overview

Eligible Designated Beneficiaries

• Disabled Persons
  – As described in IRC §72(m)(7), “an individual shall be considered to be disabled if they are unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or to be of long-continued and indefinite duration.”
  – An individual must provide proof of their disability.
  – If an individual is deemed disabled, they are allowed to use the Life Expectancy rule.
Secure Act-Overview
Eligible Designated Beneficiaries

• Chronically ill
  – As described in IRC §7702B(c)(2), a “chronically ill individual” means an individual who has been certified by a licensed health care practitioner as:
    • Being unable to perform at least two activities of daily living for a period of at least 90 days due to loss of functional capacity,
    • Having a level of disability that is to the level of the bullet point described above, or
    • Requiring substantial supervision to protect such individual from threats to health and safety due to cognitive impairment.
  – If an individual is deemed chronically ill, they are allowed to use the Life Expectancy rule.
Trusts for Disabled and Chronically Ill Beneficiaries

- Life Expectancy Treatment is Available with a “Eligible Designated Beneficiary Trust”
- Need to Draft an Accumulation Trust
- Roth IRAs may work better because the Income Tax was already paid
- Use two Trusts if you have both a traditional IRA and a Roth IRA – this avoids “trapping” the taxable IRA income
# Secure Act Beneficiary RMD Summary

<table>
<thead>
<tr>
<th>Tax Terminology</th>
<th>Designated Non-Eligible Beneficiary</th>
<th>Surviving Spouse</th>
<th>Eligible Minor Child</th>
<th>Person Less Than 10 years younger</th>
<th>Disabled or Chronically ill Person</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Outright Beneficiary</strong></td>
<td>Ten-Year Rule</td>
<td>Life Expectancy Rule</td>
<td>Life Expectancy Rule (Until Majority then Ten-Year Rule)</td>
<td>Life Expectancy Rule</td>
<td>Life Expectancy Rule</td>
</tr>
<tr>
<td><strong>Conduit Trust</strong></td>
<td>Ten-Year Rule</td>
<td>Life Expectancy Rule</td>
<td>Life Expectancy Rule (Until Majority then Ten-Year Rule)</td>
<td>Life Expectancy Rule</td>
<td>Life Expectancy Rule</td>
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<tr>
<td><strong>Designated Beneficiary Trust</strong></td>
<td>Ten-Year Rule</td>
<td>Ten-Year Rule</td>
<td>Ten-Year Rule</td>
<td>Ten-Year Rule</td>
<td>Life Expectancy Rule</td>
</tr>
</tbody>
</table>

**Footnotes:**
Stretch Out IRAs

“Inherited” IRA

Child / Grandchild Beneficiary

• Pre-Secure Act Deaths – Generally Life Expectancy if outright Beneficiary
• Post-Secure Act Deaths – Special Rules for minor Children
• Post-Secure Act Deaths – Ten-Year Rule for Adult Children and Grandchildren
Stretch Out IRAs

“Inherited” IRA

Pension Protection Act of 2006

- Beginning in 2007, non-spousal beneficiaries (e.g. children, grandchildren, friends, etc.) are permitted to roll over a qualified retirement plan (e.g. 401(k)), via a trustee-to-trustee transfer, into an “inherited” IRA
- “Designated beneficiary” trusts are also permitted to roll over qualified retirement plans to “inherited” IRAs
- Notice 2007-7

Still Available after the SECURE Act
Stretch Out IRAs

Roth Conversion of “Inherited” Qualified Plan

• Notice 2008-30 – Section II, Q&A 7, allows non-spouse beneficiaries to convert inherited qualified plans to inherited Roth IRAs.

Continues to apply after the Secure Act
Stretch Out IRAs

“Inherited” IRA

Common Mistakes to Avoid

• Incorrect titling
• Failure to take RMDs
• Failure to utilize disclaimers when appropriate
• Failure to analyze contingent beneficiaries when utilizing disclaimers
• Planning Opportunity for 2019 Deaths
  – Disclaimers to “Lock-in” Life Expectancy
• Taking a lump-sum distribution
• Not using the 10-Year “Roth Coast”
Stretch Out IRAs

“Inherited” IRA

Common Mistakes to Avoid

• Spousal rollover before age 59½
  – Will cause pre-59½ distributions to be subject to the 10% early distribution penalty
    » See Sears v. Commissioner, TC Memo 2010-146
  – If no rollover occurred, pre-59½ distributions can be taken penalty free

• Solution
  – Do not perform spousal rollover until spouse reaches age 59½

This strategy holds true after the SECURE Act
Stretch Out IRAs

“Inherited” IRA

Common Mistakes to Avoid

• For non-spousal beneficiaries, it is critical to keep the inherited IRA in the name of the deceased IRA owner.

• **Example (Individual)**
  
  – “John Smith, deceased, IRA for the benefit of James Smith”

• **Example (Trust)**
  
  – “John Smith, deceased, IRA for the benefit of James Smith as Trustee of the Smith Family Trust dated 1/1/2020”
Stretch Out IRAs

**Income in Respect of a Decedent (IRD)**

- **Income in respect of a decedent (IRD)** – is all items of gross income in respect of a decedent which were not properly included as taxable income in a tax period falling on or before a taxpayer’s death and are payable to his/her estate and/or another beneficiary. 

IRC Sec. 691(a)
Stretch Out IRAs

*Income in Respect of a Decedent (IRD)*

- **Specific Items of IRD**
  - IRAs and other qualified retirement plans
  - Unpaid salaries/wages at the time of death
  - Dividends and interest earned, but not taxed, prior to death
  - Unrecognized capital gain on an installment note at the time of the seller’s death
  - Net Unrealized Appreciation (NUA) on employer securities

NUA strategies to avoid the ten-year rule
Paying IRAs to Trusts
The Conduit Trust Disaster

• A conduit ("safe-haven") trust requires all RMDs to be distributed to the beneficiaries annually as received
• This worked well under the life expectancy rules
• However, it can be a property law disaster under the ten-year rule
The Conduit Trust Disaster

<table>
<thead>
<tr>
<th>Years after Death</th>
<th>Age</th>
<th>RMD Current Method</th>
<th>10-Year Rule Options</th>
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<tbody>
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<tr>
<td>10</td>
<td>40</td>
<td>$37,417</td>
<td>$142,378</td>
</tr>
</tbody>
</table>

Assumes $1,000,000 IRA at death & a 7% growth rate
Modifying a Conduit Trust

• When to Consider
  – Death occurs after the effective date
  – The long-term benefits of a trust are required
  – The 10-year period is locked in

• Reform or Decant
  – Remove the conduit language
  – Replace with accumulation type language

• Income Tax Planning

• Why reformations have less tax-risk
An IRA or Roth IRA Can Be Payable to a Trust

- Conduit Trust
- Accumulation Trust
- Non-designated Beneficiary Trust
- Designated Beneficiary Trust
Paying IRAs to Trusts

Issues to Review

- Designated Beneficiary Trust Status
- IRC § 642(c) Charitable Issues
- *Kenan* Issues
- IRC § 691(a) Issues
- IRC § 691(c) Issues
- Eligible Designated Beneficiary Trust Status
Legal Principals and Definitions

• Formula bequests / dispositions:
  – *Pecuniary* – gift denominated in money rather than by property; often uses formula where the amount of the gift equals a certain amount (such the estate tax exemption amount).
    • “I leave the maximum amount which will result in no estate tax to the Family Trust and the residue to the Marital Trust.”
  • Pecuniary bequests are treated as a sale or exchange of the asset distributed and causes a recognition event for the estate. *Kenan v. Comm*, 114 F.2d 217 (2d Cir. 1940); Rev. Proc. 64-19.
Legal Principals and Definitions

• Formula bequests / dispositions:
  – *Fractional* – gift by a formula which splits property by value between two takers.
    • “I leave to my spouse the residue of my estate multiplied by fraction with a numerator equal to smallest amount which will result in no estate tax and the denominator equal to the entire value of the residue.”
    • Gain or loss is not recognized upon the distribution of property to satisfy a fractional disposition.
Paying IRAs to Trusts

Four Requirements for **ALL** Designated Trusts

1. Trust is valid under state law
   • Treas. Reg. § 1.401(a)(9)-4, Q&A 5(b)(1)

2. Trust is irrevocable upon death of owner
   • Treas. Reg. § 1.401(a)(9)-4, Q&A 5(b)(2)

3. Beneficiaries of the trust are identifiable from the trust instrument
   • Treas. Reg. § 1.401(a)(9)-4, Q&A 5(b)(3)

4. Documentation requirement is satisfied
   • Treas. Reg. § 1.401(a)(9)-4, Q&A 5(b)(4)
Types of Trusts

- Accumulation Trusts
- Conduit Trusts
- Treas. Reg. § 1.401(a)(9)-4, Q&A 5 requirements apply to both types
Paying IRAs to Trusts

Conduit Trust

• A trust in which all distributions from the IRA are immediately distributed to the trust beneficiary(ies)
• Very limited asset protection
Accumulation Trust

• A trust in which distributions from the IRA are allowed to accumulate within the trust
• Stronger asset protection than a conduit trust
• The key issue in analyzing an accumulation trust is to determine which beneficiaries are “countable”
• All beneficiaries are countable unless such beneficiary is deemed to be a “mere potential successor” beneficiary
Appendixes

I. Paying IRAs to Trusts
II. Roth IRAs
III. Net Unrealized Appreciation
Paying IRAs to Trusts
Paying IRAs to Trusts

Accumulation Trust – Pre-SECURE Guidance
Example #1

- Accumulation Trust
- Sister measuring life for determining required minimum distributions
- Facts same as PLR 200228025
Paying IRAs to Trusts

Accumulation Trust – Pre-SECURE Guidance

Example #2

IRA → Trust → Child #1

At Child #1’s death

To Red Cross

- Contingent beneficiary must be counted
- Non-individual contingent beneficiary
- No designated beneficiary status
- Treas. Reg. § 1.401(a)(9)-5 Q&A 7
Paying IRAs to Trusts
Accumulation Trust – Pre-SECURE Guidance
Example #3

IRA → QTIP Trust → Spouse

All income

At spouse’s death

Issue of IRA owner in such a manner (in trust or otherwise) as the surviving spouse appoints by will

- Contingent beneficiaries must be counted
- Possible non-individual contingent beneficiaries
- General Power of Appointment disqualifies accumulation trust
Paying IRAs to Trusts

Conduit Trust

• Allows for easier identification of beneficiaries
• Where a conduit trust is used, potential appointees under a power of appointment can be ignored
• If an accumulation trust, all potential takers under a power of appointment must be considered
Paying IRAs to Trusts

Conduit Trust – Pre-SECURE Guidance

Example #1

IRA → Trust

- Discretionary distributions, but no less than total withdrawals from IRA
- Entire trust outright upon grandchildren reaching age 30
- If grandchildren die before reaching age 30:
  - Mother is not “countable” for determining applicable life expectancy
  - Treas. Reg. § 1.401(a)(9)-5 Q&A 7

Mother
Age 80

Child – Age 30

Child – Age 30
Paying IRAs to Trusts

Conduit Trust – Pre-SECURE Guidance

Example #2

IRA → Trust → Child #1

All distributions from IRA

At Child #1’s death

To Red Cross

See Treas. Reg. § 1.401(a)(9)-5 Q&A 7
Paying IRAs to Trusts

Conduit Trust – Pre-SECURE Guidance

Example #3

IRA → Trust → Child #1

All distributions from IRA

At Child #1’s death

To my lineal descendants as appointed by Child #1 in his/her last will and testament
Paying IRAs to Trusts

*Separate Share Rule*

Payable to single trust

No separate shares identified in the beneficiary designation form

IRA paid over oldest life expectancy
Paying IRAs to Trusts

Separate Share Rule

IRA payable to multiple trusts

Each trust named in beneficiary designation form

IRA paid over each separate trust beneficiary’s life expectancy

PLR 200537044
Paying IRAs to Trusts

*Post-Mortem Trust Reformations*

- In the past, IRS has respected post-mortem trust reformations that modified the trust to qualify as a designated beneficiary. See PLRs 200235038-41
- IRS no longer appears to follow post-mortem reformations
- Reformations of Conduit Trusts to Accumulation Trusts
Paying IRAs to Trusts

PLR 201021038

• Service ruled that the retroactive reformation of a trust would not be respected for purposes of section 401(a)(9) and the related regulations.
• The trustee reformed the trust pursuant to a state court order to remove charities under a limited power of appointment granted to first tier beneficiaries.
• The adverse ruling means the trust was not treated as a “designated beneficiary trust” (“DBT”) and that the trust beneficiary’s life expectancy could not be used for determining required minimum distributions.
Post-Mortem Checklist

• Deadlines
  – December 31 of year of death
    » Year of death RMD
  – Nine months after death
    » Disclaimer
  – September 30 of year following year of death
    » Beneficiary Designation determination
    » Pay off undesirable beneficiaries
  – October 31 of year following year of death
    » Documentation requirement for trusts
  – December 31 of year following year of death
    » Separate shares created
    » Begin RMDs (exception for spouse beneficiary)

• Obtain copy of beneficiary designation form
• Review beneficiary trust for potential problems/solutions
• Ensure correct titling and transfer of inherited account
• Review Disclaimers
Roth IRAs
Roth IRAs

Taxation of Distributions

• Types of Distributions
  – Qualified distributions are not subject to income tax
  – Non-qualified distributions are subject to income tax

• Basis
  – Basis can be withdrawn Tax-Free (FIFO Method)
  – Distributions are not subject to income tax if they do not exceed aggregate contributions and/or conversions to the Roth IRA
Roth IRAs

Taxation of Distributions

• Application of the 10% early withdrawal penalty
  – Withdrawals made within five years of conversion if owner is under age 59½ and no exception applies
  – Death Exception
Roth IRAs

Taxation of Distributions

• Income Taxation of Distributions – the five-year rule
  – Distributions which consist of growth of the original contribution from accounts less than five years are taxable
  – The 5-year period for all of a participant’s Roth IRAs starts on January 1 of the first year for which a contribution was made to any Roth IRA owned by that participant
  – A surviving spouse treats an inherited Roth IRA as one of her own for purposes of the five-year rule
  – The 5-year period continues to run after the participant dies
Roth IRAs

Taxation of Distributions

Roth IRA - Application of 10% Early Withdrawal Penalty
("Ordering Rules")

1. "Net contributions" is: (a) the sum of all prior Roth IRA contributions reduced by (b) the sum of all prior Roth IRA distributions (i.e. "basis first" rule).
2. Distributions attributable to prior conversion amounts are determined on a "first-in, first-out" ("FIFO") basis with the taxable portion of each prior year conversion coming out first followed by the non-taxable portion.

10% early withdrawal penalty applies (Unless exception applies)

Conversion amounts <= 5 years² (taxable portion)

Conversion amounts > 5 years² (non-taxable portion)
Roth IRAs

Taxation of Distributions

Roth IRA - Taxability of Distributions
(“Seasoning Rule”)

Is the taxpayer over age 59½? \(^1\)

- No
  - Does the taxpayer meet any of the other statutory exceptions?
    - Yes
    - Distribution subject to income tax (only to the extent of amounts not previously taxed)
    - No
      - Has the taxpayer met the five-year holding period test? \(^2\)
        - Yes
          - Entire distribution is tax-free
        - No

Footnotes:
1. IRC Sec. 408A(d)(2)(A)(i)
2. IRC Sec. 408A(d)(2)(B)
3. IRC Sec. 408A(d)(2)(A)(ii),( iii) & (iv)
   - Death
   - Disability
   - First-time homebuyer expenses (up to $10,000)
Roth IRAs

Taxation of Distributions

Roth IRA - Application of 10% Early Withdrawal Penalty
("Penalty Box Rule")

- Is the taxpayer over age 59 1/2?
  - Yes
  - No

- Is the Roth IRA:
  1. 100% contributory
  2. 100% conversion
  3. Commingled

- Is the distribution greater than prior contributions (i.e. "basis")?
  - No
  - Yes

- Did the distribution occur within five years of conversion?
  - No
  - Yes

- Follow the "ordering rules" (see above chart)

- 100% Contributory
- 100% Conversion
- Commingled

Exceptions to 10% early withdrawal penalty:
1. Death
2. Disability
3. Series of substantially equal periodic payments
4. Medical expenses greater than 7.5% AGI
5. Health insurance premiums for unemployed individuals
6. Higher education expenses
7. First-time homebuyer expenses (up to $10K)

No Penalty

Penalty applies to "earnings" (Unless exception applies)

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Roth IRAs

**Taxation of Distributions**

<table>
<thead>
<tr>
<th>Distribution within 5 years</th>
<th>Distribution beyond 5 years</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Age &lt; 59½</strong></td>
<td></td>
</tr>
<tr>
<td>Income Tax: Yes (earnings only)</td>
<td>Income Tax: Yes (earnings only)</td>
</tr>
<tr>
<td>10% Penalty: Yes (earnings &amp; taxable portion of prior conversion amounts)</td>
<td>10% Penalty: Yes (earnings only)</td>
</tr>
<tr>
<td><strong>Age ≥ 59½</strong></td>
<td></td>
</tr>
<tr>
<td>Income Tax: Yes (earnings only)</td>
<td>Income Tax: No</td>
</tr>
<tr>
<td>10% Penalty: No</td>
<td>10% Penalty: No</td>
</tr>
</tbody>
</table>
Roth IRAs

Conversion Basics

• Reasons to Convert

  1. Bracket arbitrage
  2. Increase tax-free savings by paying conversion tax with non-qualified funds
  3. Surviving spouse beneficiary is young and will not need the conversion amount for retirement – can be allowed to grow
Roth IRAs

Conversion Basics

• Reasons to Convert

4. No RMDs (in case of spouse beneficiary) prevent draining of qualified account or IRA and increase tax planning flexibility

5. Favorable tax treatment for surviving spouse – compressed single tax rates will not apply to RMDs

6. Reduces size of taxable estate

7. Ten-year payout rule for Roths allows for additional deferral
Advanced Roth IRA Planning

*Understanding the Mechanics*

• In simplest terms, a traditional IRA will produce the same after-tax result as a Roth IRA provided that
  — The annual growth rates are the same
  — The tax rate in the conversion year is the same as the tax rate during the withdrawal years (i.e. $A \times B \times C = D; A \times C \times B = D$)
## Advanced Roth IRA Planning

### Understanding the Mechanics

<table>
<thead>
<tr>
<th></th>
<th>Traditional IRA</th>
<th>Roth IRA</th>
</tr>
</thead>
<tbody>
<tr>
<td>Account Balance</td>
<td>$100,000</td>
<td>$100,000</td>
</tr>
<tr>
<td>Less: Income Taxes @ 40%</td>
<td></td>
<td>(40,000)</td>
</tr>
<tr>
<td><strong>Net Balance</strong></td>
<td>$100,000</td>
<td>$60,000</td>
</tr>
<tr>
<td>Growth Until Death</td>
<td>300.00%</td>
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<tr>
<td>Account Balance @ Death</td>
<td>$300,000</td>
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<tr>
<td>Less: Income Taxes @ 40%</td>
<td>(120,000)</td>
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</tr>
<tr>
<td><strong>Net Account Balance to Family</strong></td>
<td>$180,000</td>
<td>$180,000</td>
</tr>
</tbody>
</table>
Advanced Roth IRA Planning

Understanding the Mechanics

• Critical decision factors
  – Tax rate differential (year of conversion vs. withdrawal years)
  – Use of “outside funds” to pay the income tax liability
  – Need for IRA funds to meet annual living expenses
  – Time horizon
Advanced Roth IRA Planning

Understanding the Mechanics - Tax Rate Differential

• The key to successful Roth IRA conversions is often to keep as much of the conversion income as possible in the current marginal tax bracket

• However, there are times when it may make sense to convert more and go into higher tax brackets
Advanced Roth IRA Planning

Understanding the Mechanics - Tax Rate Differential

- 10% tax bracket
- 12% tax bracket
- 22% tax bracket
- 24% tax bracket
- 32% tax bracket
- 35% tax bracket
- 37% tax bracket

Example possible optimum Roth IRA conversion amount

Easy target Roth IRA conversion amount

Current taxable income

NIIT
Net Unrealized Appreciation (NUA) Planning & Other Issues
Tax Law Overview

- Qualified dividends are currently taxed at long-term capital gains tax rates
- Long-term capital gains tax rates
  - 0%
  - 15%
  - 20%
Tax Planning Opportunities When a Qualified Plan Has Employer Securities

• Key issues
• Income tax
• Estate tax
• Excise tax

NUA allows the Conversion of Ordinary Income to Long-Term Capital Gains
IRC § 402(d)(4)(D)  
Triggering Event

• On account of employee’s death
• After the employee attains age 59½
• On account of employee’s separation from service
• After the employee has become disabled (within the meaning of section 72(m)(7)
Net Unrealized Appreciation

• Spouse may utilize NUA
• Converts ordinary income into long-term capital gains
Taxation of Rollout

• Ordinary income recognized on basis
• Difference between Fair Market Value (FMV) at rollout and basis is Net Unrealized Appreciation (NUA)
• NUA is taxed long-term capital gain tax rates
Taxation of Net Unrealized Appreciation

Fair Market Value (FMV) of stock $ 750,000
Employer basis $ 150,000
Net Unrealized Appreciation (NUA) $ 600,000
Amount taxable if stock is rolled out $ 150,000
The $600,000 of NUA is Deferred Until the Stock is Sold
Additional Taxation of Rollout

• If under age 55 a 10% excise tax penalty is imposed on the basis of the securities
A Key Issue is the Proper Holding Period to Obtain Capital Gain Treatment
Post Distribution Gain

• 1 year or less -- Short-term
• Greater than 1 year -- Long-term
Treatment at Death

• The $600,000 of rollout gain does not receive a step-up in basis
• Subsequent gain (above $600,000) should receive a step-up in basis
Treatment at Death

• If the estate or trust contains NUA stock, a fractional funding clause must be used. Otherwise, the NUA will be subject to immediate taxation.
IRA Distributions are Taxed at the Taxpayer’s Marginal Tax Bracket
Lump-Sum Distribution Treatment

• Generally a 100-percent lump sum is not feasible from a financial planning perspective
Post-Mortem Rollover Solution

• Surviving Spouse Rolls over
• Easy to implement
• Easy to understand
• Allows Surviving Spouse to create a balanced portfolio
Rollover Solution

• Disadvantages
  – Pre-59½ rules
  – No capital gain treatment
  – Limits estate tax planning options