ASK THE EXPERT: Answers to Common Questions About IRA Trusts

By: The Ultimate Estate Planner

The IRA Inheritance Trust® (also known as a "Standalone Retirement Trust", "IRA Beneficiary Trust" or just plain and simple "IRA Trust") has now been around for over 10 years. The IRS approved this strategy in PLR200573044 and, even though, it's been around for some time, it's only now that so many estate planners are starting to implement and use this planning for their clients.

Whether it's fear of learning something new, not fully understanding or being clear about the benefits for using this trust strategy, or just not having ever heard of it, it is clear that there is definitely still some mystery or misunderstandings about IRA Trusts.

We are focusing this article on answering the top five questions we receive about standalone IRA Trusts. And, what better way than to get these answers from IRA Trust Expert and IRA Inheritance Trust® creator himself, Philip J. Kavesh.

IRA TRUST QUESTION #1: Why is a standalone IRA Beneficiary Trust a better planning option than a Revocable Living Trust?

ANSWER. There are both technical and practical reasons why an IRA Beneficiary Trust is a better planning option than leaving IRA assets to the Living Trust.

First, here are the technical reasons:

1. There are a number of regular provisions in a living trust that will disqualify it as a designated beneficiary trust, such that the beneficiaries will not be able to use their own life expectancy for calculating required minimum distributions ("RMDs") and may be forced to use a life expectancy as short as 5 years. These provisions include but are not limited to payment of debts, expenses and taxes, accounting for principal and income, and charitable beneficiaries.

2. Although it is possible to firewall some or all of these provisions when a beneficiary is given a conduit trust (that pays out all RMDs immediately to the beneficiary), the process of firewalling becomes much more complicated if an accumulation trust (which offers significant asset protection) will be used.

3. Since a standalone IRA Trust with the toggle switch feature can allow the protective benefits of an

accumulation trust if needed in the future and the free-standing IRA Inheritance Trust® has already received a PLR stating it qualifies as a designated beneficiary trust, if total IRAs (husband and wife) exceed a $150,000, it makes more sense to use this standalone trust than take the risk that a 5-year RMD rule could apply and that future protection may be lost. See PLR 200537044.

Second, here are the practical reasons why a standalone IRA Trust is a better planning option than a Living Trust:

1. The standalone IRA Trust, in its very first page, is clearly established to meet the requirements of a designated beneficiary trust, so it's much easier for a custodian to read, understand and implement it. When these designated beneficiary trust provisions are buried inside a larger living trust, it often winds up with the custodian delegating their decision to their legal department which can hold up the process of implementing the trust in a timely manner.

2. By having a standalone IRA Trust, it alerts the beneficiaries to the fact that IRAs have special treatment and makes it less likely that the beneficiaries (including a beneficiary that may be serving as Trustee) will immediately go to the custodian and cash out the IRA or take other actions that may have adverse tax consequences. When we do our IRA Inheritance Trust®, it comes with a checklist of actions for the Trustee and beneficiary to follow, in order to avoid these types of inadvertent mistakes.

At the end of the day, with the Supreme Court decision in the *Clark v. Rameker* case, a standalone IRA Trust is highly recommended to better protect your clients' hard-earned IRA assets when they are inherited.

IRA TRUST QUESTION #2: For a married couple, do you draft a joint trust or separate trusts?

ANSWER. With a long-term married couple, with no children of another marriage, each spouse would typically get his or her own individual IRA Inheritance Trust® for his or her own IRAs. The trusts would be mirror images of one another and each spouse would typically name the other as the primary beneficiary and the subshares of his or her own IRA Trust as secondary beneficiaries. This way, the surviving spouse may do a favorable rollover of IRAs into his or her name, and then be able to name his or her own IRA Trust (the beneficiaries' subshare trusts) as beneficiary and still have the option to change beneficiaries and how and when they will receive their inherited IRAs because the surviving spouse's IRA Trust can be revocable and amendable. The first spouse to die's IRA Trust becomes irrevocable at death, as prescribed by the IRS Regulations.

IRA TRUST QUESTION #3: Do you typically draft IRA Beneficiary Trusts as conduit or accumulation trusts?

ANSWER. Unless there are known asset protection concerns with respect to one or more of the beneficiaries, then we typically draft IRA Trusts as a conduit to guarantee the maximum stretchout benefit. One of the unique features of our IRA Inheritance Trust® is that the IRS approval of the "toggle switch" provision, which allows you to toggle from a conduit to an accumulation trust if additional asset protection is needed. But, if we know, at the time of drafting, that an accumulation trust is appropriate for asset protection reasons, then we will use it because there is some risk in relying upon the toggle switch to be done properly and timely.

IRA TRUST QUESTION #4: How do you complete the Beneficiary Designation Form and have you had any trouble getting an IRA Custodian to accept or approve the IRA Trust strategy?

ANSWER. The way that we typically complete the beneficiary designation form ("BDF") is as follows:

This example is for the BDF for the Husband of a married couple that have four children.

PRIMARY BENEFICIARY:

100% [WIFE'S NAME]

SECONDARY BENEFICIARY:

25% [CHILD #1 NAME] TRUST*

25% [CHILD #2 NAME] TRUST*

25% [CHILD #3 NAME] TRUST*

25% [CHILD #4 NAME] TRUST*

[AT BOTTOM OR SOMEWHERE ON THE FORM]

*established as a separate share trust under the [HUSBAND'S NAME] IRA Inheritance Trust® dated [TRUST DATE]

Dealing with IRA Custodians can sometimes be a hassle, because it all depends on who you get to speak with and what they believe is allowable and what is not. We've had some IRA Custodians deny a BDF simply because there wasn't enough room to put that kind of information in their system. We've had some IRA Custodians allow us to add an addendum to the BDF to explain the subshare trusts and the IRA Inheritance Trust®. We've also had some IRA Custodians request hold harmless language to protect them since this is out of their norm.

Only in a few cases have we had to get more involved with an IRA Custodian, which usually involves speaking with their legal department to really straighten it out, by showing them a copy of the Private Letter Ruling. Usually once they see that the IRS has approved this strategy, they're more cooperative and willing to accept the BDF.

For a sample BDF and hold harmless language previously used with some IRA Custodians, click here.

IRA TRUST QUESTION #5: What are the benefits of an IRA Beneficiary Trust over some of the other planning options available, such as a Trusteed IRA or Restricted Annuity Beneficiary Payout?

ANSWER. The major benefits of an IRA Beneficiary Trust over a Trusteed IRA or the Restricted Annuity Beneficiary Payout options are an added level of asset protection, while retaining the greatest level of flexibility to adjust as needed that level of protection.

For a more thorough and in-depth comparison of these three techniques with a side-by-side chart comparing each strategy's features, please see the article entitled, "Ensuring the Stretchout".

These are just some of the common questions that come up, but there are many other questions and issues that people have experienced when it comes to drafting IRA Beneficiary Trusts. Unfortunately, we cannot get to all of them in this particular article, but most (if not all) of the major technical issue and drafting concerns are addressed in our upcoming 90-minute educational program entitled, "The Traps & Tricks of Drafting IRA Beneficiary Trusts", scheduled for **Thursday, March 17, 2016 at 9am Pacific Time (12pm Eastern Time).** For more information and to register, click here.

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