Samantha Davis -Trusts and Designating Beneficiaries for Retirement Assets

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Many estate planning clients have retirement plan assets which include individual retirement accounts and 401(k) plans. As advisors, we are tasked with assisting clients on the best way to transfer these assets to beneficiaries in a manner consistent with their estate plan. Most qualified retirement plans are taxable which is typically different compared to other assets the client owns. It is key that the beneficiary designation forms be completed correctly and appropriate language exists in the trust to achieve the estate planning objectives.

When a client has a revocable trust, the issue of coordinating designating beneficiaries can be complicated and can result in an accelerated income tax liability. Only naming individuals on designation forms is easy and can result in a maximum deferral period. However, many non-tax reasons exist for naming trusts as a beneficiary of qualified retirement assets such as asset protection, special needs planning, maturity of beneficiaries, etc. Steps can be taken help to provide for a longer applicable distribution period or "stretch".

The Treasury Regulations lack some clarity on which beneficiaries should be considered when applying the rules to determine the beneficiary with the shortest life expectancy for the applicable distribution period using some trusts.

More recently, in 2016, the IRS released PLR 201633025 (May 18, 2016) ruling that some contingent beneficiaries named in a trust (i.e. settlor's siblings and charities in this case) will not be taken into account for purposes of determining the applicable distribution period and are deemed "mere successor beneficiaries within the meaning of the regulations." The result is very favorable for the taxpayer as the settlor's child's life expectancy is used in determining the applicable distribution period. If the siblings and charities would have been taken into account, the likely outcome is that the trust would not be deemed to have a "designated beneficiary" under the Treasury Regulations because the charities are not "individuals" and result in shorter deferral period.

Until the IRS provides greater clarity, one planning route may be draft the trust document to assume that the IRS may take into account all contingent beneficiaries. Another option is a separate revocable trust as a beneficiary of only qualified retirement assets. However, all facts and options should be considered to help achieve client goals. Hopefully, a future revenue ruling on point will be forthcoming.

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Practices

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