Retirement Benefits in the Non-Taxable Estate: Maximizing Tax-Deferred Advantages

Estate Planning for Pension and 401Ks, IRAs/Roth IRAs, Beneficiary Designations, and Post-Mortem Administration

TUESDAY, FEBRUARY 24, 2015
1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

Today’s faculty features:

Bruce Givner, Principal, Givner & Kaye, Los Angeles
Kristen M. Lynch, Shareholder, Fowler White Burnett, Fort Lauderdale, Fla.

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Trust & Estate Teleconference

Retirement Benefits in the Non-Taxable Estate: Maximizing Tax-Deferred Advantages, Estate Planning for Pension and 401k’s, IRAs/Roth IRAs, Beneficiary Designations and Post-Mortem Administration

February 24, 2015

PANELISTS:
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The purpose of this informative webinar is to provide some background on qualified plans and IRAs, as well as how they fit into planning for non-taxable estates.

The speakers will discuss the types of IRAs and qualified plans, planning issues that can arise and will discuss best practices and approaches towards correcting the problems or mitigating the damage caused, including:

• The impact of ERISA and REA on plan beneficiary designations;
• The deadlines after death within which actions should be taken;
• How to preserve or salvage tax deferral/life expectancy if possible;
• Spousal IRA concerns – community property, divorce settlements, elective share;
• Post-mortem possibilities if the named beneficiary has “Special Needs”;
• The issues presented when trusts are named or utilized inappropriately;
• The constant balance between best possible tax deferral and getting the IRA into the right hands; and
• Best practices
Why Planning with Qualified Plans and IRAs is Important

• Maximize use of Estate Tax exemption (where needed)
• Coordinate estate plan under will or revocable trust
• Generally, the IRA or qualified plan is the largest asset of the estate
• Minimize income tax on distributions and thereby maximize deferral
Qualified Plans typically offered by “for profit” businesses:

• Defined benefit
• Defined contribution
• Employee Stock Ownership Plan (ESOP)
• Self-Employed Pension (SEP)
• Keogh
Tax Qualified Employee Retirement Plan

Joe

Owner

The corporation (Plan Sponsor)

Employees/participants

The Plan

Plan committee

The Trust

Trustee

$
Qualified Plans typically offered by “tax exempt” businesses:

- 403(b) plan
- 457 plan
Types of IRAs:

• Contributory
• Rollover
• Roth
• Inherited IRA
• MyIRA
What Federal Laws Govern Qualified Plans & IRAs?

– Internal Revenue Code requirements

– IRC §401 – Distribution Rules

– Other Tax Law – Income Tax, Estate Tax, GST

– Bankruptcy Law

– Private Letter Rulings, Revenue Rulings, etc.
What State Laws Govern IRAs and can effect Qualified Plans?

– Uniform Principal and Income Act

– Guardianship

– Intestacy Statutes

– Elective Share, Divorce, Pre-Post Nuptials or Community Property

– Asset Protection

– Case Law
Typical Contractual Provisions for IRAs and Qualified Plans

- Qualified plans must be surviving spouse if covered by ERISA
- Beneficiary default language for IRAs (estate versus surviving spouse)
- Per stirpes versus per capita
- Payout options during lifetime and post-mortem
- Governing law
- Arbitration clauses
IRC §408 and §408A - requirements

- IRA custodians and trustees must be approved by the IRS;
- IRA documents must be pre-approved by the IRS, and must be updated for regulatory changes much like qualified plans whenever the government requires it;
- IRAs must contain certain standard language, but may be customized for business purposes;
- IRAs are either “trustee’d” (managed) or “self-directed”;
- Non-compliant custodians and trustees may have their approval to serve revoked.
IRC §401 – Distribution Rules

• Applies to both qualified plans and IRAs;
• Required distributions begin upon attainment of age 70 ½ by the IRA Owner, or upon the death of the IRA Owner, depending upon what happens first;
• Different rules depending on whether IRA Owner died before age 70 ½ or after;
• Different rules depending on whether there is a “designated beneficiary” or not;
• Different rules depending on whether the IRA is a Roth or not.
## 401(a)(9) Regulations

### Single Life Table

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Post-death critical questions:
• Did the participant die before his RBD?
• Is the spouse the sole beneficiary?
• Are there multiple beneficiaries?
• Are all beneficiaries “designated beneficiaries”? 
• What does the IRA/qualified plan allow?
Post-death RMDs based on whether “designated beneficiary” exists:

– Only “individuals” with quantifiable life expectancy can be “designated beneficiaries”

– If trust qualifies, look through to underlying trust beneficiaries

– Distribution out of trust to beneficiary does not make the beneficiary the “designated beneficiary”
## 401(a)(9) Regulations

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<td><strong>Non-Designated Beneficiary</strong></td>
<td>Five-Year Rule</td>
<td>Owner’s “Ghost” Life Expectancy Rule</td>
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02/24/2015 Lynch/Givner Teleconference
401(a)(9) Regulations

• 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
401(a)(9) Regulations

• A designated beneficiary determines his/her RMD life expectancy factor by reference to 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 (This is otherwise known as the “subtract one” method)
401(a)(9) Regulations

The Final Regulations created some new opportunities for post-mortem planning.

New critical dates:

- **September 30th** of the year following the year of death:
  - Date at which the beneficiaries are identified

- **October 31st** of the year following the year of death:
  - Date at which trust documentation (in the case where as trust is named as a designated beneficiary) must be provided to custodian

- **December 31st** of the year following the year of death:
  - Date at which the first distribution must be made by each IRA beneficiary, and
  - Date at which separate shares must be created
The Final Regulations (cont.):

• If there is one “non-designated” beneficiary left on September 30th, no beneficiaries get separate share treatment and distributions are based on the single non-recalculated life expectancy of the decedent.
401(a)(9) Regulations

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
  - Allows for distributions to remove unwanted beneficiaries
  - Allows for time to divide the account if there is a problem

- If a beneficiary dies before the September 30 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)
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

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.
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.
Slide Intentionally Left Blank
Disclaimer Planning

Disclaimer must be “qualified”:

• In writing

• Within 9 months of date of death of decedent

• No acceptance of the interest or any of its benefits (does not include receipt of RMD that decedent was required to take in year of death)

• Interest passes without any direction on the part of the person making the disclaimer
Generation Skipping Tax Issues

- GST implications should be considered before disclaimer is executed.

- Disclaimers should be used to fully utilize GST exemption.
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

PLR 201202042

• Father died after naming a trust for the benefit of Mother as beneficiary of his IRA.

• Mother died 11 days after Father.

• Mother’s executor disclaimed Mother’s interest in trust and in IRA.

• After Mother’s death, trust was for the benefit of child and grandchild.

• IRS – RMDs from IRA can be taken over child’s life expectancy, as oldest beneficiary of trust.

• Disclaimer eliminated Mother as countable beneficiary of trust.
Practical Question:

Who is going to be responsible for ensuring all the deadlines are met according to schedule?

More importantly, who is liable if they are not?
Practical Problems under the Final Regulations:

- The post mortem planning opportunities occur with the ability to disclaim, distribute or divide the assets.
- To disclaim, it must be done in compliance with section 2518 and must generally be done within nine months of the decedent’s date of death — this is not extended to the September 30th beneficiary determination deadline.
- To distribute to a beneficiary that is not a “designated” beneficiary and not have it throw off everyone else in the mix, this must be done prior to September 30th.
- If the accounts are going to be set up in separate accounts, the accounts must be set up by December 31st of the year after death but must be determined by the September 30th deadline.
Spouse as “Designated” Beneficiary:

• May roll over into their own name and make new 70½ elections regardless of their age when they inherit, or may change name on the account.

• May leave IRA in name of decedent and continue distribution method in place.
Trust as “Designated” Beneficiary:

- IRA owner must provide a list of the trust beneficiaries to the IRA custodian or Trustee has until October 31 of year after IRA owner’s death to provide trust document or list of beneficiaries, although to be practical the trustee or custodian should have the documentation prior to the September 30 determination date;

- Trust must be valid under State law;

- Trust must become irrevocable by its own terms upon the death of the IRA owner;

- Beneficiaries must be easily identifiable through the trust document.
Why Designate a Trust as Beneficiary?

• The reasons are the same with IRAs and qualified plans as they are with other estate assets:

  – Minor beneficiaries (avoids guardianship);
  – Special need beneficiaries (avoids guardianship and can preserve Medicaid benefits);
  – Spendthrift beneficiaries;
  – Second or multiple marriages;
  – “Significant other” beneficiaries;
  – Beneficiaries with substance abuse problems;
  – Estate tax purposes (to preserve credit shelter or marital deduction).
Other Considerations in Naming a Trust as Beneficiary:

• For treatment as separate shares, two requirements must be met:
  – The interests of the beneficiaries must be expressed as fractional or percentage interests as of the date of death of the IRA owner; and,
  – Separate accounts must be established by December 31st of the year after the IRA owner’s death.

• This is important because without separate share treatment, the trust will be limited to using the life expectancy of the oldest beneficiary. If the goal was to pay the IRA to separate sub-trusts, this may be a trap for the unwary.
Other Tax Law – Income Tax, Estate Tax, GST

• All distributions from IRAs and QRPs are subject to income tax
  – Contributory and roll over IRAs as distributions are made;
  – ROTH IRAs prior to contribution or at time of conversion.

• IRAs and QRPs are included in estate tax calculations, and are subject to exemption amounts for estate tax and generation skipping tax.

• IRAs and QRPs are considered Income in Respect of a Decedent.
Sample Beneficiary Designation Form

ABC Corporation Profit Sharing Plan Beneficiary Designation Form

If you die before receiving any of your retirement benefits, your beneficiary will be your spouse if you are married on the date of your death and you have been married to your surviving spouse for at least one year. Unless an alternative form of benefit is selected by you (with spousal consent if required) on the Benefit Distribution Request Form, at your retirement, you and your spouse will receive a joint and 50% survivor annuity.

If you die before receiving any of your retirement benefits and you are not married or have been married to your spouse for less than one year on the date of your death, your beneficiary will be the person you have designated as a beneficiary; if you have not designated a beneficiary, your beneficiary will be your surviving spouse, surviving children, your parents or your estate, in that order. Unless an alternative form of benefit is selected by you or your beneficiary, your beneficiary may receive a single sum payment of the balance in your account.

If you die after you begin receiving payment of your retirement benefits, your beneficiary will receive a benefit in accordance with the form of benefit that you elected to receive before your death.
Complete this Form only if you would like to make a beneficiary designation different from that which is stated above. If you are a Beneficiary who is entitled to receive benefits under the Plan due to the death of a Participant, please complete this section and Section 1-A as if you were the Participant. (Please print or type.)

Participant Name: ______________________________________________
Social Security Number: _________________________________________
Daytime Phone Number: _________________________________________
Mailing Address: ________________________________________________

I. BENEFICIARY DESIGNATION – Participant MAY Complete A and B Below To Designate Specific Beneficiary(ies).

A. Beneficiary Designation (Please print.)

Primary Beneficiary(ies) – I hereby designate as my primary beneficiary(ies):

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<tr>
<th>Name</th>
<th>Address</th>
<th>Relationship</th>
<th>% Share</th>
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</thead>
<tbody>
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<td></td>
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<td>100 %</td>
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</tbody>
</table>
Sample Beneficiary Designation Form [continued]

Secondary Beneficiary(ies) – If my primary beneficiary(ies) predecease me, I designate as my secondary beneficiary(ies):

<table>
<thead>
<tr>
<th>Name</th>
<th>Address</th>
<th>Relationship</th>
<th>% Share</th>
</tr>
</thead>
</table>

________
100%

SIGNED _______________________________ Date _______________________________
Participant

B. Filing Status (Check One.)

Note: If you are in the process of divorce, you are still considered married.

1. _____ I am single. (Stop here. Do not complete the rest of this form.)

2. _____ I am married and have designated my spouse as the primary beneficiary of 100% of my account balance. (Stop here. Do not complete the rest of this form.)

3. _____ I am married, but I am entitled to benefits under this Plan as the Beneficiary of a Participant who has died. (Stop here. Do not complete the rest of this form.)

4. _____ I am married and have designated my spouse as the primary beneficiary of less than 100% of my account balance. (If you checked this option, read Section IV and complete Section II.)
Sample Beneficiary Designation Form [continued]

II. WAIVER OF SPOUSAL DEATH BENEFIT
Participant MUST complete A and B below if Box 4 in Section I-B was checked.
A. Waiver
   I have read the Notice of Spousal Death Benefit in Section IV explaining the spousal death benefit available to my spouse under the plan. Understanding the terms of this benefit, I voluntarily elect to waive the spousal death benefit. I understand that I am subject to the conditions of my spouse’s consent to this waiver unless I have been married to my spouse for less than one year.

   If I have been married for less than one year, this election will remain in effect until such election has been revoked or until I have been married to my spouse for one year or more, whichever is earlier.

   SIGNED ___________________________________________ Date ________________________________
   Participant

B. Spousal Information (Check One.)

1. ______ My spouse consents to my beneficiary designation(s) and waiver. (If you checked this option, your spouse must read Section IV and complete Option A or B of Section III.)
Sample Beneficiary Designation Form [continued]

2. _____ I am married but my spouse’s written consent to this election is not required because:
   
a. [ ] I have been married to my spouse for less than one year.

b. [ ] My spouse cannot be located. I agree to inform the Plan Administrator if the location of my spouse becomes known.

c. [ ] My spouse and I are legally separated and a copy of the court order to that effect is attached. (Note: A qualified domestic relations order may require you to obtain your spouse’s consent.)

d. [ ] My spouse has abandoned me and a copy of the court order to that effect is attached.

(If you checked this option, stop here. Do not complete the rest of this form.)

III. SPOUSAL CONSENT
Spouse MUST sign waiver and have signature witnessed below if Box 1 in §II-B was checked.

Option A. Specific Consent (Caution: Read Notice of Spousal Death Benefit re: Specific Consent.)

I, ____________________, am the spouse of ________________. I understand that I may have the right to the preretirement survivor annuity (“PSA”) and joint and survivor annuity (“JSA”) benefits from the Plan upon my spouse’s death. I agree to give up the right to ___% of the account and to have that amount paid to the beneficiaries designated in Section 1.
Sample Beneficiary Designation Form [continued]

I understand that my spouse cannot change the name of any beneficiary in the future unless I agree to the change.

I understand that, by signing this agreement, I may receive less money than I would have received under the special PSA and JSA payment forms and I may receive nothing from the Plan after my spouse dies.

I understand that I do not have to sign this agreement. I am signing this agreement voluntarily.

I understand that if I do not sign this agreement, then I will receive the JSA or PSA benefit (whichever is applicable) upon my spouse's death. I understand that if the value of the PSA benefit is $5,000 or less, the Plan will pay the benefit to me in one lump sum payment.

I agree to release and discharge the Plan, the Trust, the Administrator and other Plan representatives, and ABC Corporation, its officers and employees from liability for acting pursuant to this consent.

SIGNED ________________  Date ________________
Spouse
Sample Beneficiary Designation Form [continued]

Witness of Spousal Consent
Spousal consent MUST be witnessed by a Notary Public OR an Authorized Company Representative.

Witnessed by a Notary Public -OR- Witnessed by an Authorized Company Representative
Subscribed and sworn before me this
____ day of _____________, 200____

Notary Public ______________________
State of ___________________________
My commission expires ______________

Authorized Company Representative
SIGNED____________________________
Date _____________________________

Option B. General Consent (Caution: Read Notice of Spousal Death Benefit re: General Consent.)

I, ___________________________________, am the spouse of _________________________________.
Participant's Spouse

I understand that I may have a right to the preretirement survivor annuity (“PSA”) and joint and survivor
annuity (“JSA”) benefit forms.
Sample Beneficiary Designation Form [continued]

I agree to give up _______% of the account and to have that amount paid to someone else as the beneficiary. I understand that by signing this agreement, my spouse can choose the beneficiary without telling me and without obtaining my agreement. I also understand that, by signing this agreement, my spouse can change the beneficiary at any time before retirement benefits begin without telling me and without obtaining my agreement.

I understand that, by signing this agreement, I may receive less money than I would have received under the special PSA and JSA payment forms and I may receive nothing from the Plan after my spouse dies.

I understand that I can limit my spouse's choice to a particular beneficiary who will receive the vested account balance and that I am giving up that right.

I understand that I do not have to sign this agreement. I am signing this agreement voluntarily.

I understand that if I do not sign this agreement, then I will receive the JSA or PSA benefit (whichever is applicable) upon my spouse's death. I also understand that if the value of the PSA benefit is $5,000 or less, the Plan will pay the benefit to me in one lump sum payment.
Sample Beneficiary Designation Form [continued]

I agree to release and discharge the Plan, the Trust, the Administrator and other Plan representatives, and ABC Corporation, its officers and employees from liability for acting pursuant to this consent.

SIGNED ___________________________________________ Date ________________

Spouse

Witness of Spousal Consent

Spousal consent MUST be witnessed by a Notary Public OR an Authorized Company Representative.

Witnessed by a Notary Public -OR- Witnessed by an Authorized Company Representative

Subscribed and sworn before me Subscribed and sworn before me
this ____ day of ________, 200__ SIGNED____________________________

Notary Public ______________________________ Authorized Company Representative
State of ______________________________
My commission expires __________________
IV. NOTICE OF SPOUSAL DEATH BENEFIT

The Notice of Spousal Death Benefit is directed to the Participant's spouse and should be read by both the Participant and his or her spouse. This notice describes spousal rights and the spousal death benefit, the Participant's right to waive them, and his or her spouse's rights regarding any such waiver.

In general, if the Participant dies before the commencement of benefits, the Plan must automatically pay a spousal death benefit based upon the Participant's account balance to your surviving spouse (if any) as beneficiary, provided the Participant has been married to his or her spouse for at least one year as of the date of the Participant's death.

Waiving the Spousal Death Benefit

If the Participant has been married to his or her spouse for at least one year, the spouse of the Participant will be paid an annuity bought with 100% of the Participant's account balance, unless:

- the Participant waives the spousal death benefit by completing Section II of this form, and,
- the Participant's spouse voluntarily consents to both the Participant's waiver (in Section II) and the indicated designated beneficiary(ies) by completing Option A or Option B of Section III of this form.
Sample Beneficiary Designation Form [continued]

Note: Even if the current beneficiary is a trust or estate of which the Participant's spouse is the sole beneficiary, the waiver and spousal consent are necessary. Without such waiver and consent, the spousal death benefit must be paid directly to the spouse of the Participant.

To: The Participant's Spouse

It is important that you and your spouse understand your rights and obligations concerning your death benefits. You may direct any factual questions to the Plan Administrator. However, you should consult your legal and/or financial advisor to determine what is best for your particular situation.

1. What Rights Do You Have to Benefits After Your Spouse Dies?

Your spouse has an account in the ABC Corporation Profit-Sharing Plan (“Plan”). The money in the account that your spouse will be entitled to receive is called the vested account. If you have been married to your spouse for at least one year as of the annuity starting date, defined as the first day of the first period for which a benefit is payable as an annuity, the Plan is required to pay retirement benefits in a special payment form unless your spouse chooses a different beneficiary or payment form and you agree to that choice. The special payment form is often called a “joint and survivor annuity” or “JSA” payment form. The JSA payment form gives your spouse a monthly retirement payment for the rest of his or her life. This is often called an “annuity.” Under the JSA payment form, after your spouse dies, each month, the Plan will pay you a percentage of the retirement benefits that was paid to your spouse. The benefit paid to you after your spouse dies is often called a “survivor annuity” or a “survivor benefit.” You will receive this survivor benefit for the rest of your life.
Sample Beneficiary Designation Form [continued]

Example
Pat Doe and Pat's spouse, Robin, receive payments from the Plan under the JSA payment form. Beginning after Pat retires, Pat receives $600 each month from the Plan. Pat then dies. The Plan will pay Robin, on a monthly basis, a percentage of $600 for the rest of Robin's life.

Further, if you have been married to your spouse for at least one year as of your spouse's date of death, the Plan gives you the right to receive a special death benefit if your spouse dies before he or she begins receiving retirement benefits (or, if earlier, before the beginning of the period for which the retirement benefits are paid). You have the right to receive this monthly payment for your life beginning after your spouse dies. This special death benefit is often called a “preretirement survivor annuity” or “PSA” benefit. The Plan will pay this death benefit in a lump sum, rather than a PSA, if the value of the death benefit is $5,000 or less.

2. Can Your Spouse Choose Other Beneficiaries to Receive the Account?

Generally, your right to the JSA and PSA benefit cannot be taken away unless you agree to give up that benefit. If you agree, your spouse can choose to have all or part of the vested account paid to someone else. In addition, if you have been married for less than one year, your spouse may choose to have all or part of the vested account paid to someone else. This choice by your spouse remains valid until such election is revoked or you have been married to your spouse for a year. Each person your spouse chooses to receive a part of the vested account is called a “beneficiary.” For example, if you agree, your spouse can have the vested account paid to his or her children instead of you.
Sample Beneficiary Designation Form [continued]

Example

If you have been married to your spouse for at least one year, your spouse cannot have the vested account paid to someone else unless you agree and sign this agreement.

4. Do You Have to Give Up Your Right to the JSA and PSA Benefit?

Your choice must be voluntary. It is your personal decision whether you want to give up your right to the special JSA and PSA payment forms.

5. Can Your Spouse Change the Beneficiary in the Future if You Sign this Agreement?

You have the right to agree to allow your spouse to select only a particular beneficiary or to allow your spouse to select and change at any time the beneficiary who will receive all or part of the vested account without informing you and without obtaining your agreement.

If you want to allow your spouse to select only a particular beneficiary, select Option A - “Specific Consent” of the spousal consent agreement in Section III. If you select and sign Option A - “Specific Consent” in Section III, your spouse cannot change the beneficiary named in this agreement to anyone other than you, unless you agree to the new beneficiary by signing a new agreement.
Sample Beneficiary Designation Form [continued]

If you want to allow your spouse to select and change at any time the beneficiary of the vested account without your agreement, select Option B - “General Consent” of the spousal consent agreement in Section III. If you select and sign Option B - “General Consent” in Section III, your spouse can choose the beneficiary who will receive all or part of the vested account without informing you and without obtaining your agreement. Your spouse can change the beneficiary at any time before the account is paid out.

5. Can You Change Your Mind After You Sign this Agreement?

You can change this agreement until the date on which you or your spouse begin receiving payments from the Plan. After that date, you cannot change the agreement. If you change your mind, you must notify the Plan Administrator and complete a new Beneficiary Designation Form.

6. What Happens to this Agreement if You Become Divorced?

You may lose your right to the PSA and JSA benefit if your spouse and you become legally separated or divorced even if you do not sign this agreement. However, if you become legally separated or divorced, you might be able to get a special court order (which is called a qualified domestic relations order or “QDRO”) that specifically protects your rights to the vested account. If you are thinking about getting a divorce, you should obtain legal advice on your rights to benefits from the Plan.
Individual Retirement Account (IRA) Beneficiary Designation Form

Please print in all CAPITAL LETTERS and use black ink. This form designates or amends beneficiary(ies) for all types of IRAs. This form supersedes all previous designations. The beneficiary designation will apply to all of your John Hancock mutual funds within the IRA type(s) indicated by you below. Each of the undersigned agrees to indemnify John Hancock Signature Services, Inc. and John Hancock Funds, LLC against any fees, claim or expense (including reasonable attorney’s fees) to the extent that any transfer effected pursuant to these instructions is alleged or found for any reason to have been invalid or ineffective, and transfer is subject to the condition that John Hancock Signature Services, Inc. and John Hancock Funds, LLC will be entitled to attach or debit the account of the IRA beneficiary to the extent necessary to enforce their rights to this indemnity.

1. Shareholder Information

Owner’s Name (first) [ ] (M) [ ] (L.J.)

Social Security Number (required) [ ] Date of Birth (MM/DD/YYYY)

2. IRA Type

☐ Traditional IRA  ☐ Roth IRA  ☐ Simple IRA  ☐ SARSEP  ☐ SEP

3. Mailing Address

Address [ ] [ ]

City [ ] State [ ] Zip [ ]

Phone Number [ ]

4. Beneficiary Designation (all information must be completed)

- John Hancock Funds reserves the right to round up fractional shares for distribution.
- Designating beneficiaries is an important part of the estate planning process. Please take care in choosing your beneficiaries and, of course, make plans to periodically review your beneficiaries to make sure nothing should change. We have provided some basic information about this process below; however, if you have specific questions regarding how this will affect your estate plan, we recommend that you contact your tax adviser or estate attorney.
- You may change your beneficiary(ies) at any time after the initial designation by notifying John Hancock Signature Services, Inc., in writing.
- If no beneficiaries are designated, or if there are no beneficiaries living at the time of your death, your estate will generally be entitled to your account assets.
- Percentages for beneficiaries must total 100% for each section. If not, transfers shall be made proportionally on the percentages stated. If no percentages are indicated, each primary beneficiary who survives you will receive equal percentages of your account.
- If multiple beneficiaries are listed and a beneficiary does not survive you, his or her percentage will be divided equally among the remaining beneficiaries, unless previously stated otherwise.
- Contingent beneficiaries are entitled to receive your account only if there are no surviving primary beneficiaries at the time of your death.
- For Trusts, please list the Trust name, name of Trustees and Trust establishment date.
- John Hancock Funds allows you to place certain restrictions on distributions made to your named beneficiaries. In order to take advantage of this feature, please leave this section blank and complete the John Hancock Funds Individual Retirement Account (IRA) Restricted Beneficiary Designation Form available by calling John Hancock Signature Services, Inc. at 800-225-5291 or by visiting our Web site at www.jhfunds.com.
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<th>Relationship to Owner</th>
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<td>TOTAL: _________________________</td>
<td>(Must add up to 100%)</td>
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Spousal Consent — Required if your spouse is not named as sole primary beneficiary and you reside in a community or marital property state. You should consult with your own legal or tax adviser to determine if spousal consent is required.

I am the spouse for the above-named IRA account owner. I acknowledge that a designation of a non-spouse beneficiary may not be effective in my state without my consent. I hereby consent to the beneficiary designation(s) stated above.

Signature of Spouse ____________________________ Date (MM/DD/YYYY)

5. Signature

- The terms and conditions of this beneficiary designation are construed and administered according to the laws of the Commonwealth of Massachusetts.
- Any addition to, deletion from or change to this form is void unless approved in writing by John Hancock Funds.

X Signature of Account Owner ____________________________ Date (MM/DD/YYYY)

6. Mail

Please enclose and mail to:

<table>
<thead>
<tr>
<th>Regular mail: Mutual Funds Operations</th>
<th>Express mail: Mutual Funds Operations</th>
</tr>
</thead>
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<tr>
<td>John Hancock Signature Services, Inc.</td>
<td>John Hancock Signature Services, Inc.</td>
</tr>
<tr>
<td>P.O. Box 55913</td>
<td>30 Dan Road</td>
</tr>
<tr>
<td>Boston, MA 02205-5913</td>
<td>Canton, MA 02021</td>
</tr>
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</table>

1-800-225-5291 1-800-554-6713 TDD 1-800-338-8080 EASH-Line 529 College Savings Plan
Mutual Funds Privately Managed Accounts Retirement Plans
www.jhfnurs.com

NOT FDIC INSURED, MAY LOSE VALUE, NO BANK GUARANTEE, NOT INSURED BY ANY GOVERNMENT AGENCY.
Bankruptcy Protection for Inherited IRA

- In order for a retirement account to fall under the exemption of Sec. 522(b)(3)(C), two elements must be present:
  - the amount the debtor seeks to exempt must be retirement funds; and
  - those retirement funds must be in an account that is exempt from taxation under IRC Sections 401, 403, 408, 408(A), 414, 457, or 501(a).

- Question: Do retirement funds held in a traditional IRA account lose their character upon the death of the account owner before the funds pass to a non-spouse beneficiary?

- Supreme Court determined that funds held in an IRA with a non-spouse beneficiary were not retirement funds after the death of the account owner for the purposes of the exemption.

- The Court however did not address whether the spousal beneficiary of an IRA of a dead account owner was protected from creditors by the exemption.
Florida’s Elective Share (as an example)

• The elective share statute provides that the spouse can elect to take 30% of the “elective estate”, which has now been expanded to include death benefits payable under qualified and non-qualified retirement plans.

• This includes amounts payable by reason of the decedent’s death under any public or private pension, retirement, or deferred compensation plan, or similar arrangement.

• A transfer is excluded from the elective estate if it is made with the written consent of the surviving spouse. This includes ERISA spousal waivers.
Florida’s Elective Share (Continued)

- Subject to a priority system, all direct recipients of property included are liable for contribution toward satisfaction any remaining unsatisfied balance of the elective share, with the liability being proportional to the proportional part of the elective estate received.

- Unless there is an extension, the elective share election must be filed by the earlier of six months from receipt of the notice of administration or two years after the decedent’s date of death.
Issues Presented by the Elective Share

• State law versus Federal law — this involves the Supremacy clause of the Constitution and will be a question of whether ERISA will trump the probate code in regard to qualified plans.

• Timeline issue — what if an IRA beneficiary takes distribution before an election is made and has already taken on the tax liability? How will this be corrected?
Issues Presented by the Elective Share (Continued)

• In regard to waivers, is the spouse made aware when signing an ERISA waiver for a qualified plan that this will pre-empt elective share election of this asset even when rolled into an IRA? Most states have statutes defining what constitutes an “informed” waiver.

• How does someone account for IRAs that contain both rollover monies that have had an ERISA waiver and regular contributions? Some will be elective share and some will not. Seems counter to EGGTRA intent.
Community Property, Pre-Nuptials & Post-Nuptials

- Via agreement between both spouses under state law
  - Example: Wisconsin Marital Property Agreement
- Reclassification of account
  - Prenuptial and postnuptial
  - Example: from individual property to marital property or from community/marital property to individual property
Community Property, Pre-Nuptials & Post-Nuptials

• **PLR 8929046**
  - A transaction in which a wife transmuted her community property interest in her husband's IRA in return for his community property interest in other assets was not subject to income tax.

• **PLR 199937055**
  - IRS allows IRA to be classified as community property pursuant to a community property agreement. Taxpayer then proposed to transfer the community property interest in IRA to spouse. IRS would treat the transfer as a taxable distribution.

• **PLR 20021501**
  - Husband and wife entering into a post-nuptial agreement that provided for the division of an IRA at divorce will not be considered a prohibited transaction under IRC Sec. 4975(c) or cause a loss of exemption with respect to the IRA IRC Sec. 408(e)(2)(A).
Community Property Exchange

- PLR 199925033
  - The non-pro rata partition of community property in a trust and the allocation of an IRA to a survivor's trust is neither a sale or exchange under section 1001, nor a transfer under section 691.

- PLR 201125047
  - Marital property exchange facilitated spouse rollover of entire IRA.
Community Property Exchange

- Spouses may provide in a community/marital property agreement that at the death of a spouse some or all of their community/marital property will be divided based on aggregate value rather than divided item by item.

- Surviving spouse and successor in interest to the decedent's share of community/marital property may enter into an agreement providing that some or all of the community/marital property in which each has an interest will be divided based on aggregate value rather than divided item by item.
Disposition at Death After Divorce


- Decedent and wife divorced. In divorce, the wife gave up her right to any retirement plan. Decedent, however, did not remove ex-wife as beneficiary of his plan.

- Held - The plan administrator did its ERISA duty by paying the benefits to decedent’s ex-wife as the named beneficiary in conformity with the plan documents.

- ERISA preempted the marital settlement agreement and preserved the former spouse’s rights in the plan account.

- The beneficiary could disclaim ERISA benefits without violating anti-alienation rule.
Disposition at Death After Divorce


- State law automatically revoked a former spouse's status as beneficiary of an employee's interest in non-probate assets following a divorce.

- In this case, the assets was a death benefit under a policy of life insurance.

- Held: State law that tries to establish rules by which an ERISA plan must distribute benefits is preempted.

- **Moral of the Story** – Clients must change the beneficiary after a divorce if they do not want their ex-spouse to obtain the benefits.
Disposition at Death After Divorce

• IRA – Dependent on State Law and IRA Custodial Agreements

• Many IRA custodial agreements will treat an ex-spouse as predeceased if couple were divorced after beneficiary designation form completed

• Many states have precedential case law that determines if an ex-spouse is named on the most recent beneficiary designation, they are entitled to the IRA regardless of whether the IRA owner had remarried.

• Some states have statutes stating that divorce nullifies a beneficiary designation form that names a spouse as beneficiary
Example:

- Husband rolled over community property qualified plan to IRA
- IRA adoption agreement had a provision that if the participant's spouse was not named the sole primary beneficiary, the spouse would have to sign a consent.
- Husband named trust which provided income to wife for life, remainder to children as beneficiary of IRA.
- Wife signed consent which read: "Being the participant's spouse, I hereby consent to the above designation."
- When wife died, the executrix of her estate sought to assert a community claim against the IRA accounts.
- Held: Consent of the wife was ineffective for transmutation of her community rights and her estate could claim her community interest in the IRA, despite evidence she intended that it pass according to the beneficiary designation.
When the Estate is Beneficiary:

- As discussed earlier, estates are not considered designated beneficiaries. Even so, there is good news within the final regulations. Under the new rules, an estate may use the remaining single non-recalculated life expectancy of the IRA owner if the IRA owner died after attaining age 70½. The old rule was that the IRA had to be distributed by December 31st of the year after the IRA owner’s death. This new rule means that even if some disaster occurs where disclaimers and distributions will not work to fix a bad beneficiary designation (or perhaps no designation at all), there is still some time for deferral.
When the Estate is Beneficiary (cont.):

• If an estate is the beneficiary of an IRA, it is made clear in the final regulations that even if the estate is then distributed out to the ultimate beneficiaries, there is no additional life expectancy gained by doing so. Because the estate is not considered a designated beneficiary, it does not matter who ultimately receives the IRA assets (other than for income tax purposes) because they will be limited to deferral based on the remaining single non-recalculated life expectancy of the IRA owner at the time of their death.

• BEWARE OF BEING SURCHARGED!
Asset Protection without Bankruptcy

• **ERISA Protection**
  - Exempt from claims of creditors
  - Sole employee and spouse exception

• **State Law Protection**
  - Some states offer protection similar to ERISA
  - Some states offer limited protection
California Code of Civil Procedure
Exemption From A Money Judgment Creditor
§704.115. Private retirement plans; exemption; periodic payments

(a) As used in this section, "private retirement plan" means:

(1) Private retirement plans, including, but not limited to, union retirement plans.

(2) Profit-sharing plans designed and used for retirement purposes.

(3) Self-employed retirement plans and individual retirement annuities or accounts provided for in the Internal Revenue Code of 1986, [FN1] as amended, including individual retirement accounts qualified under §§408 or 408A of that code, to the extent the amounts held in the plans, annuities, or accounts do not exceed the maximum amounts exempt from federal income taxation under that code.

(b) All amounts held, controlled, or in process of distribution by a private retirement plan, for the payment of benefits as an annuity, pension, retirement allowance, disability payment, or death benefit from a private retirement plan are exempt.
(d) After payment, the amounts described in...(b) and all contributions and interest thereon returned to any member of a private retirement plan are exempt.

(e) Despite (b) and (d), except as provided in (f), the amounts described in ¶(3) of (a) are exempt only to the extent necessary to provide for the support of the judgment debtor when the judgment debtor retires and for the support of the spouse and dependents of the judgment debtor, taking into account all resources that are likely to be available for the support of the judgment debtor when the judgment debtor retires. In determining the amount to be exempt under this subdivision, the court shall allow the judgment debtor such additional amount as is necessary to pay any federal and state income taxes payable as a result of the applying of an amount described in ¶(3) of subdivision (a) to the satisfaction of the money judgment.
Recent Developments

Commerce Bank, N.A. v. Bolander
(2007 WL 1041760 (Kan. App. 2007))

• Revocable trust named as beneficiary of IRA.

• Trust became irrevocable at death of IRA owner.

• Ruling: IRA subject to deceased IRA owner’s creditor claims because trust was revocable before death.
## IRAs at Death

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<thead>
<tr>
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<td>Excellent</td>
<td>Life Expectancy</td>
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Disposition at Death

- Qualified Plans
- Anti-Alienation Rule
- Non-employee spouse’s community/marital property interest in plan terminates at death
- Non-employee spouse does not have testamentary disposition power over plan

- Example:
  - Alex owns a qualified plan through his employer. Alex and his wife, Lydia, live in a community property state and one-half of Alex’s qualified plan is considered Lydia's property under the community property laws of their state. Lydia dies before Alex. Under the terminable interest rule, Lydia’s interest in Alex’s qualified plan ends at her death.
Disposition at Death

• State property law preempted by ERISA

• Deceased non-employee spouse has no testamentary property rights in employee spouse’s qualified plan, other than those provided by ERISA.

• Surviving nonemployee spouse might lose any marital property interest in deceased’s deferred employee benefit plan if the beneficiary killed the decedent. However, ERISA may preempt the state slayer statute.
What Controls if there is a Conflict?

- Sometimes federal law control;
- Sometimes state statutes control;
- Sometimes contractual provisions control;
- Sometimes case law controls.

- Protects the interests of participants and beneficiaries in private-sector employee benefit plans.

- Supersedes state laws relating to employee benefit plans except for certain matters such as state insurance, banking and securities laws, and divorce property settlement orders by state courts.

- An employee benefit plan may be either a pension plan (which provides retirement benefits) or a welfare benefit plan (which provides other kinds of employee benefits such as health and disability benefits).

- ERISA sets standards that pension plans must meet in regard to:
  - who must be covered (participation),
  - how long a person has to work to be entitled to a pension (vesting), and
  - how much must be set aside each year to pay future pensions (funding).
Types of Qualified Retirement Plans

- ERISA and the IRC classify employer-sponsored retirement plans as either defined benefit (DB) plans or defined contribution (DC) plans.
- A defined benefit plan specifies either the benefit that will be paid to a plan participant or the method of determining the benefit.
- A defined contribution plan is one in which the contributions are specified, but not the benefits.
Corporation (plan sponsor)

Money goes in – define (limit) the contribution

Retirement Trust

Money goes out – define (limit) the benefit

Employee/Participant
If you limit how much goes **in** (IRC Section 415(c) - $49,000), then there is no limit on how much goes **out**. So if you are going to buy Qualcomm at $1 and have it go to $100, do so in a defined contribution plan; it will not impact your future contributions.
If you limit how much goes **out** (IRC Section (b), (d) - $195,000), there is no specific limit on how much goes in. So if you want a contribution of more than $49,000 per person, you need a defined **benefit** pension plan.
The Retirement Equity Act of 1984 (REA)

• Amended ERISA to increase pension protections for the survivors of deceased plan participants.

• As amended by the REA, ERISA requires defined benefit plans and money purchase plans to provide preretirement and postretirement survivor annuities to married employees unless a written election to waive the survivor annuity is signed by both the employee and his or her spouse.
REA (Continued)

• Made a lifetime annuity with a survivor annuity for a spouse the default form of benefit from traditional pension plans for married workers.
• If a married worker wishes to receive a lifetime annuity for him or herself, rather than a reduced lifetime annuity with a survivor annuity, he or she must obtain the consent of his or her spouse.
• A spouse's consent to a QPSA waiver is effective only if it:
  • Is in writing;
  • Acknowledges the effect of the waiver;
  • Consents to a designated beneficiary; and
  • Is witnessed by a plan representative or notary public.
REA (Continued)

• A spouse may give either general or specific consent to a designated beneficiary.
  – General consent permits the participant to change a beneficiary without further spousal consent.
  – Specific consent means that the spouse consents to a specific beneficiary for the QPSA and new consent must be given if a different beneficiary is named.

• Spousal consent is not required if:
  • The participant is unmarried;
  • The spouse cannot be located; or
  • There is a court order stating that the participant is legally separated or has been abandoned by the spouse.
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QTIP Issues

QTIP-IRA
Key QTIP-IRA Rulings

• Rev. Rul. 89-89
• Rev. Rul. 2000-2
• Rev. Rul. 2006-26
QTIP Issues

QTIP-IRA

- Qualifying for the marital deduction
- Definition of “income”
- Qualifying as a “designated beneficiary” trust
QTIP Issues

QTIP-IRA

- Direct transfers to spouse
- QTIP trusts
- Community property
- REA waiver
  - Does not apply to IRAs
  - Rollover from ERISA plan to IRAs does not carryover the REA waiver rights – Charles Schwab v. Debickero, No. 07-15261, CA-6 (1/22/2010).
QTIP Issues

QTIP-IRA Sources of "Income"

• Income from assets titled in the trust
• Income from assets titled in the IRA
QTIP Issues

QTIP-IRA

Fiduciary Accounting Income vs.
Tax Accounting Income

• Fiduciary accounting income is governed by state law and the trust instrument

• Tax accounting income is governed by the federal income tax law
QTIP Issues

QTIP-IRA
Typical Types of “Income” Under Traditional Fiduciary Accounting

• Interest
  - Taxable
  - Tax-exempt
• Dividends
• Rents (net of expenses)
• Royalties
QTIP Issues

QTIP-IRA
Typical Types of “Principal” Under Traditional Fiduciary Accounting

- IRA value as of date of death
- Increases in asset value (i.e. growth)
- Realized long-term capital gain
- Realized short-term capital gain
- Proceeds from covered call writing
QTIP Issues

QTIP-IRA Income (Rev. Rul. 2006-26)

- Traditional fiduciary accounting income
- Equitable adjustments under UPIA §104(a)
- Unitrust payments
- “10% rule” under UPIA §409(c)
- “Savings clause” under UPIA §409(d)
QTIP Issues

QTIP-IRA
Equitable Adjustment

• UPIA §104(a) provides trustees the power to adjust between income and principal if a trust cannot be administered fairly between the income and remainder beneficiaries

• **NOTE:** Revenue Ruling 2006-26 holds that, notwithstanding a trustee’s application of UPIA §104(a), a trust will qualify the marital deduction
QTIP Issues

**QTIP-IRA Unitrust Payment**

- Revenue Ruling 2006-26 approves unitrust trust payments paid pursuant to UPIA §409(c) under applicable state law.

- **Example:** IRA is valued at $1,000,000. Pursuant to state law, the trust makes a unitrust distribution of 4% ($40,000). In this case, the $40,000 is a qualified “income” interest.
QTIP Issues

**QTIP-IRA**
**UPIA “10% Rule”**

- UPIA §409(c) provides that 10% of IRA (and other qualified plan) distributions are considered to be “income”

- **Example:** RMD from IRA is $40,000. Pursuant to UPIA §409(c), $4,000 ($40,000 x 10%) is considered to be “income”.

- **WARNING:** This type of clause may not qualify as “income” under Rev. Rul. 2006-26.
QTIP Issues

QTIP-IRA Savings Clause

• UPIA §409(d) provides trustees the discretion to make additional payments in order to qualify the payments as “income” for purposes of the marital deduction.

• **WARNING:** This type of clause may not save the QTIP election under Rev. Rul. 2006-26.
Stretch Out IRAs

“Inherited” IRA

**Objective:** Prolong IRA payments over longest possible period of time, thus increasing wealth to future generations
“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 the tax law the IRA assets can be distributed based upon the life expectancy of the beneficiary.
Stretch Out IRAs

“Inherited 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
Stretch Out IRAs

“Inherited” IRA

Spousal Beneficiary

• Marital deduction should be available

• Typically the default

• If no rollover is chosen, then the life expectancy factor of spouse is used by reference to the Single Life Table beginning in the year the IRA owner would have turned age 70½. Each year thereafter the life expectancy divisor is recalculated by referencing the Single Life Table.
Stretch Out IRAs

“Inherited” IRA

Spousal Beneficiary - Rollover

• Exception to Inherited IRA rules.
• Only available to surviving spouse.
• Allows spouse to roll over 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.
Stretch Out IRAs

“Inherited” IRA

Child / Grandchild Beneficiary

• Utilizes the exception to the five year rule
• Avoids IRA assets being subject to estate tax in spouse’s estate
• Achieves “Inherited IRA” to the degree that distributions occur over life expectancy of the designated beneficiary
Stretch Out IRAs

“Inherited” IRA

Child / Grandchild Beneficiary

- Life expectancy of child and/or grandchild determined in year after year of the IRA owner’s death by reference to the Single Life Table and then is reduced by a value of one each subsequent year.
Paying IRAs to Trusts

Benefits of Utilizing a Trust

- Spendthrift protection
- Creditor protection
- Divorce protection
- Special needs
- Investment management
- Estate planning
- “Dead-hand” control
Paying IRAs to Trusts

Disadvantages of Utilizing a Trust

- Trust tax rates
- Legal and trustee fees
- Trust income tax returns
  - 1041
  - 1099
  - K-1
- Greater complexity
Four Requirements for **ALL** 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)
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
Paying IRAs to Trusts

Accumulation Trust

• A trust in which distributions from the IRA are allowed to accumulate within the trust

• Stronger asset protection than a conduit trust
Accumulation 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.
Paying IRAs to Trusts

Conduit Trust

Allows for easier identification of beneficiaries
Paying IRAs to Trusts

Conduit Trust

Lineal descendants can be ignored because all distributions are paid through the trust to Child #1.
Paying IRAs to Trusts

Common Mistakes to Avoid

• Older or unidentifiable contingent beneficiary
• Estate as contingent beneficiary
• Powers of appointment
• Failure of beneficiaries clause
• Failure to provide trust document to custodian by October 31 of year following year of death
• Making lump sum distribution to trust
• General powers of appointment
• Tax issues
• Asset protection issues
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.
How to Fix “Broken” Irrevocable Trusts

• What would cause an irrevocable trust to be in need of repair?  
  – Events that could not be anticipated by the original Grantor, such as:
    • Change in family circumstances:
      – Births
      – Deaths
      – Marriages
      – Divorces
      – Special Needs Issues
      – Spendthrift Issues
      – Substance or alcohol abuse
      – Lack of beneficiary maturity at mandatory distribution ages
How to Fix “Broken” Irrevocable Trusts

– Competing interest of beneficiaries that could not be foreseen;
– Falling out with or death of successor or current trustees;
– Trustee powers are too restrictive;
– Unfavorable state law governing trust;
– Inconvenient trust situs;
– Drafting errors in document that create ambiguities;
– Changes in tax law or unanticipated tax issues
How to Fix “Broken” Irrevocable Trusts

• How do we determine what options are available?
  – Look to the trust document:
    • Does the Trustee or Trust Protector have powers to correct the problem granted in the document?
    • Does anyone have a limited power of appointment over trust property that could effectively resolve the problem?
    • Does the trust document provide any express provisions for modification?
How to Fix “Broken” Irrevocable Trusts

• If no solutions are found in the trust document, consider:
  – Decanting
  – Judicial Modification
  – Non-Judicial Modification
Paying IRAs to Trusts

Reforming Beneficiary Designations

- PLR 200616039-41 - Daughter's life expectancy could be used. Even though no contingent beneficiaries were named, court reformed beneficiary designation to name daughters as contingent beneficiaries of IRA.

- IRS is currently rethinking this position.
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
Paying IRAs to Trusts

Separate Share Rule

PLR 200537044

- **Ruling 1:** Each Beneficiary’s Trust Share Qualified for Maximum Stretch-out.
  - Upon the death of the Settlor, the IRA stand-alone trust creates separate shares for each beneficiary (in this case, separate shares for 9 beneficiaries), each trust share “treated effective ab initio to the date of the Decedent’s death” and each share functioned as a “separate and distinct trust” for the beneficiary.
  - The beneficiary designation form named each separate share as a primary beneficiary of the IRA.
  - Before the December 31st deadline, the IRA was divided into separate accounts for each share.
  - **Held:** Separate account treatment permitted; MRD of the IRA for each separate trust share measured by the lifetime of its sole beneficiary for whom the share was created.
Paying IRAs to Trusts

Separate Share Rule

PLR 200537044

- **Ruling 2:** Allowance of One-Time “Toggle” Between Accumulation and Conduit Trust.
  - Each separate share in the IRA stand-alone trust had language structuring the separate share as a conduit trust.
  - The trust provided for an independent 3rd party, as “trust protector” to transform each sub-trust to an accumulation trust in the protector’s sole discretion by voiding the conduit provisions *ab initio*.
  - Trust Protector had the authority to limit the initial trust beneficiary *ab initio*.
  - After Participant’s date of death, Trust Protector exercised “toggle” and converted one share to an accumulation trust.
  - **Held:** Each share can use that the life expectancy of its initial beneficiary to measure the MRD for that share.
Ruling 3: Payment of Expenses from IRA not considered an accumulation.

- The trust provided that “Trust expenses may be deducted prior to any such payment to or for the benefit of the beneficiary of the trust share if the deduction does not disqualify the status of the trust as a conduit trust. This paragraph may be rendered void, ab initio, by the Trust Protector.”
- Held: Each share can use that the life expectancy of its initial beneficiary to measure the MRD for that share.
- Why? Even with the deduction for payment of trust expenses, no amounts distributed to the trust during the beneficiary’s lifetime would be accumulated in the trust, and thus would not be kept in the trust for the benefit of any future beneficiaries. Treas. Reg. § 1.401(a)(9)-5 Q&A 7(c)(3), Example 2.
Paying IRAs to Trusts

Separate Share Rule

PLR 200537044

• **Ruling 4:** The trust assets will not be included in the estate of the primary beneficiary of a share upon that beneficiary’s death.
  – Each trust share would accumulate the net income of the trust, and distributions of income and principal could distribute accumulated income and principal to the primary beneficiary for his or her health, education, maintenance and support only.
  – The document did not grant any beneficiary a general power of appointment over his or her share.
  – Held: The provisions of the trust could not result in estate inclusion for the estate of a primary beneficiary upon his death.
Paying IRAs to Trusts

Pecuniary Bequests to Charity
CCA 200644020

• Pecuniary bequest to charitable beneficiary

• Acceleration of income

• No 642(c) deduction - terms of trust did not direct or require that the trustee pay the pecuniary legacies from the trust's gross income
Paying IRAs to Trusts

Pecuniary Bequests to Charity Proposed Regulations

• Prop. Regs. § 1.642(c)-3(b)(2) and § 1.643(a)-5(b)
• A provision in the governing instrument or in local law specifically providing the source out of which amounts are to be paid controls for Federal tax purposes to the extent such provision has economic effect independent of income tax consequences.
• In the absence of such specific provisions in the governing instrument or in local law, the amount to which section 642(c) applies is deemed to consist of the same proportion of each class of the items of income of the estate or trust as the total of each class bears to the total of all classes.
Thank you for your attention.

For answers to all of your IRA and QRP questions, please contact us:

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