

The “Daily Plan-It™”

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Two Smart Things To Do with an Inherited IRA Part I

The IRS recently issued two important private letter rulings about inherited IRAs. One allows for the creation of “separate shares” for a trust beneficiary, if the plan participant has named his trust as the beneficiary of the IRA. The other allows the beneficiary to transfer his interest in an inherited IRA to his trust. However, as we shall see, each case involved sloppy planning, and the plan participant could have done better. In today’s newsletter, we’ll look at the first option.

Distributions to Trust Beneficiaries

As we discussed in a previous newsletter, an IRA holder can name a revocable living trust as the beneficiary of an IRA. If done correctly, as a general rule, distributions will be based upon the life expectancy of the oldest beneficiary of the trust.

Last year, the IRS issued PLR 200537044, which authorized splitting an IRA into “separate shares” for beneficiaries of a trust after the plan participant’s death, with each share to be distributed to an individual trust beneficiary. In other words, if the trustmaker created a trust with four beneficiaries, and named the trust as beneficiary of his IRA, upon the plan participant’s death, the trustee could split the IRA into four separate shares and designate one of the trust beneficiaries as beneficiary of each IRA. Each beneficiary would then take distributions based upon his life expectancy.

Benefiting large families

This is a very valuable estate planning strategy, especially for people with blended families and large age differences between their children. The downside is that it requires some clean up after the plan participant’s death. For participants with large IRAs, it makes more sense to split each IRA into as many IRAs as there are trust beneficiaries, and to name each as beneficiary of one IRA.

This way, there’ll be no doubt about calculating required minimum distributions to the beneficiary on the plan participant’s death.

Protecting your children

Further, the IRA owner should consider creating a stand-alone IRA trust as beneficiary of the IRA, rather than naming an individual. If someone is an IRA beneficiary, the IRA will be distributed to him outright. This may or may not be in the best interests of the beneficiary, or what the plan participant wanted. After all, how many parents trust their 19-year-old’s financial acumen? If a trust for the benefit of the child is named as beneficiary, rather than the child outright, the child’s inheritance can be protected from his lack of judgment, and, if the trust has a spendthrift clause, from the claims of the child’s creditors, as well.

Part II will appear in the next issue.

Hoopes & Adams, PLC

From time to time, Hoopes & Adams hosts estate and business succession planning workshops to provide education on options, issues and concerns.

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John Hoopes and Ron Adams are the founding members of Hoopes & Adams, PLC, an estate planning and business law firm. Their principal goal is to ensure clients and their loved ones are able to care for themselves and their family while alive and well and in the event of disability, and to then provide clients the confidence of knowing they are able to leave their estate to whom they want, when they want and in the way they want, all with fully disclosed and controlled settlement and administration costs.