

## **SHOULD YOU NAME A TRUST AS BENEFICIARY OF YOUR RETIREMENT PLAN?**

Do you want your children or others to inherit your individual retirement accounts (IRAs) and your 401(k) or other qualified retirement plans, but you'd like to control the distribution of those assets after you die? Naming a trust as beneficiary of your retirement accounts may be an answer.

Various IRS rulings and revised minimum distribution rules have made the designation of trusts as beneficiaries a far more attractive option than before, but it has to be done right to work.

First, of course, you must decide whether designating a trust as beneficiary makes sense. For example, say you have minor children or adult children incapable of wisely managing your retirement plan assets. If you name them directly as beneficiaries of the retirement accounts, they may choose to withdraw and spend all of the assets as soon as they become available. But funnel the assets through a qualified beneficiary trust and you can maintain significant control for years by restricting the amount of assets available annually—as well as defer taxation.

To qualify as a designated beneficiary trust, a trust must meet four criteria:

- It must be valid under state law
- It must be irrevocable at the death of the grantor
- It must have natural individuals as beneficiaries—estates, charities and corporations generally do not qualify
- It must certify to the retirement plan or IRA administrator the trust's beneficiaries no later than October 31 of the year following the owner's death

By meeting these criteria, the retirement account administrators can “look through” the trustee to the trust's named beneficiaries as though they had been named as direct beneficiaries by the accounts' owner.

While all trusts can be beneficiaries of retirement accounts, being qualified as a designated beneficiary trust is important because it can take advantage of the minimum distribution rules set down by the IRS in early 2001. Under those rules, the minimum distribution that must be made annually from an inherited retirement account is based on the

1. Beneficiary's age, or the age of the oldest beneficiary in the case of multiple beneficiaries
2. New Uniform Life Table, which takes into account longer life expectancies, consequently reducing the minimum amount the beneficiary must take out.

A qualified trust acts as beneficiary of these minimum distributions and the trustee in turn passes them on to the named beneficiaries of the trust. But the trustee isn't required to pass on more than the minimum distribution, thus preventing heirs from rapidly depleting a retirement account. Generally, estate planners use revocable living trusts, which become irrevocable upon the owner's death, as designated beneficiary trusts, though some other trusts can be used.

With unqualified trusts, the payouts are determined by the life expectancy of the account owner if the owner has already begun minimum distributions (around age 70 1/2). For owners who die before starting minimum distributions, all assets in the account would have to be distributed by the trust within five years.

Exactly how you set up the trust will depend on several factors, including the size of the estate, the spouse's age, and the number of beneficiaries and their ages. For example, if you have a large estate, you may want to name the spouse as the primary beneficiary and the children as contingent beneficiaries; otherwise, you could have significant income- and estate-tax liabilities if the trust is the primary beneficiary.

As you might expect when dealing with trusts, careful planning and drafting of the trust document is essential. To begin with, clarify whether a given retirement account administrator (especially employer-sponsored plans) will allow the account assets to go to the trust. Second, don't name any beneficiaries, even as contingent beneficiaries, that don't qualify as "natural" beneficiaries. Although charities generally do not qualify as natural beneficiaries, it is possible to name a charity to a designated beneficiary trust under certain conditions, but the trust must be drafted properly to allow for this. Multiple beneficiaries also require additional trust design decisions.

All in all, naming a trust as a beneficiary of your retirement plans can be an effective estate planning tool, but like all estate planning strategies, it must be carefully compared with other options and carefully designed if chosen.