Estate Preservation Law Offices

BRIDGING THE GAP

between traditional estate planning and asset protection

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Practice Areas

Estate Planning
Asset Protection Planning
Elder Law and Medicaid Planning
Business and Corporate Planning
Special Needs and Disability Planning
Estate and Trust Administration
Guardianships and Conservatorships
Tax Planning: Corporate and Individual
Charitable and Exempt Organizations
Equine and Pet Trust Planning
Veterans Benefits Planning
Financial Aid Planning

Locations

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For our clients' convenience, we also have offices in Braintree and Hyannis, MA

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Estate Planning for Retirement Accounts: Have your Cake *and* Eat It Too

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For many of us, "qualified retirement accounts" such as IRAs and 401Ks make up the bulk of our retirement savings. These accounts, which are funded with pre-tax earnings and grow income tax-free, are great vehicles for saving and investing, but pose a unique challenge in the estate planning process.

Because qualified retirement accounts are funded with pre-tax dollars, distributions that are later taken from the accounts are fully income taxable to the recipient – both to you during your life as the original account owner/contributor, and to your beneficiaries after your death.

In a typical retirement scenario, qualified retirement accounts are used to supplement retirement income and are spent slowly over a

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Frequently Asked Questions

Spotlight on The Retirement Trust

In the article above, we introduced a specially-designed Retirement Trust for owners of qualified retirement accounts who wish to protect the inheritance of their children or other beneficiaries. The Retirement Trust uses the life expectancy of the individual beneficiaries inside the trust to stretch retirement account distributions over the life expectancy of the individual(s), which minimizes income taxes, achieves tax-free growth and protects the account and the annual distributions from financial threats the beneficiary may face.

Since the Retirement Trust is a relatively new technique, most individuals and even many financial and legal professionals are not familiar with how it works. Read on for answers to common questions about Retirement Trusts and learn how simple it is to add a Retirement Trust to your existing estate plan or to integrate a Retirement Trust as part of a new estate plan.

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Retirement Accounts *Continued from page one*

period of years. When the original account holder reaches age 70 ½, he/she must begin taking "required minimum distributions" (RMDs) from the account – and as the money comes out, the income taxes get paid. Most owners avoid taking more than the RMD to minimize the income tax obligation in any one year and maximize the tax-free growth of the account.

Upon the owner's death, the retirement account passes automatically to the beneficiaries named by the owner when he/she set up the account. If a spouse is named he/she may elect a "spousal rollover" and continue deferring distributions until 70 ½. All other non-spousal beneficiaries have two options: 1) take a lump-sum distribution and pay all the income taxes at once, or 2) establish an "inherited IRA," which allows the new owner to take RMDs calculated on the basis of his/her actuarial life expectancy. Clearly the latter is a better option for income tax planning (taxes paid in any one year will be minimal because withdrawals are stretched over a long period of time) and retirement savings (the account balance continues to grow tax-free).

Now for the estate planning challenge: statistically, inherited money is spent at a substantially faster rate than earned or saved money. This means that after the account holder dies, children and other beneficiaries are more likely than not to withdraw the account in one lump sum, pay all the income taxes at once, and spend the money. For the average beneficiary, the damage consists of a huge tax hit and a loss of potential future earnings – not an ideal result, but not the end of the world.

But what about beneficiaries who are financially vulnerable because they are young, disabled/receiving benefits, struggling with an addiction, facing bankruptcy or on the verge of a divorce? The safest option in these cases is to designate a trust for such person's benefit rather than naming the person directly as beneficiary. However, IRS regulations only permit a "designated beneficiary" to stretch the withdrawals over a beneficiary's life expectancy, and most trusts do not meet this requirement. Bottom line: the trust would have to withdraw the account funds over a shortened period of time – as few as five years – resulting in higher income taxes and loss of tax-free growth.

Now for the estate planning challenge: statistically, inherited money is spent at a substantially faster rate than earned/saved money.

This poses a tough choice for qualified retirement account owners: Do you name your beneficiaries directly so they will have the option of using their life expectancy to stretch the distributions, but risk them losing the account to impulsive spending or third parties (creditors, divorcing spouses, etc.)? Or do you protect the inheritance inside a trust for your beneficiaries, but knowing they will end up paying higher income taxes and losing the long term tax-free growth?

The good news is that there is now a third option: name a special "Retirement Trust" that qualifies as a "designated beneficiary." This allows the life expectancy of the individual beneficiaries inside the trust to be utilized to stretch the account distributions to the trust over the life expectancy of the individual(s), thereby minimizing income taxes, achieving long-term tax-free growth and protecting the account and distributions from financial threats the beneficiary may face.

If you have a qualified/pre-tax retirement account, take the time to think about your intended beneficiaries and whether they may be financially vulnerable based on age, marital status, health/disability, financial acumen, personal or professional activities that may expose them to lawsuits, prior bankruptcies or judgments, or any other reason. If so, you should consider establishing a Retirement Trust as part of your estate plan. Even if you have done Roth conversions on your IRAs, there are still RMD components and post-conversion taxable growth with which to contend.

The good news is that there is now a third option: name a special "Retirement Trust" that qualifies as a "designated beneficiary."

The attorneys at Estate Preservation Law Offices are happy to meet with both current and potential clients on a complimentary basis to review your existing retirement account beneficiary designations and make recommendations based on your planning goals and the needs of your intended beneficiaries.

Special Needs Planning

The Role of Retirement Trusts in Special Needs Planning

With the changing landscape of retirement, many families have become more aggressive in funding their pre-tax/qualified retirement accounts. At the same time, the number of families with special needs planning concerns is on the rise with the increased incidence of certain diagnoses and more individuals participating in means-tested programs such as Medicaid and SSI (Supplemental Security Income).

Families engaged in special needs estate and financial planning face particular challenges when it comes to retirement accounts because of the complicated IRS regulations governing qualified retirement account distributions and how the accounts must be structured to achieve maximum income tax deferral (see Estate Planning for Retirement Accounts on page one).

The focus of special needs planning is to provide for special needs beneficiaries while enabling them to become or remain eligible for means-tested benefits. By way of example, programs such as Medicaid (in certain circumstances) and SSI mandate that participants have no more than $2,000 of "countable assets" in their own name. These and other programs such as subsidized housing also have income limits for participants. Parents, grandparents or other relatives of special needs individuals will typically incorporate one or more special needs trusts into their estate plans for the assets to be left to the special needs child or grandchild so that these individuals can be included as beneficiaries of the estate without having their inheritance considered part of their assets for program purposes.

A properly-drafted special needs trust can be named as a beneficiary of a qualified retirement account for a special needs beneficiary's portion of the account and prevent the asset from disrupting program benefits. However, a typical special needs trusts will not qualify as a "designated beneficiary" under the IRS regulations, resulting in a higher income tax obligation and the loss of long term tax-free growth on the retirement account.

Creating a Retirement Trust to receive the qualified retirement account assets of a beneficiary's inheritance is a sound way to enhance special needs planning. Because of the care needs and future challenges that many special needs beneficiaries face, it is critical that their inheritances be preserved and grown to the extent possible to ensure they receive the maximum benefit from these funds.

In creating a Retirement Trust for a special needs beneficiary, it is important to work with attorneys who understand both the rules governing qualified retirement account distributions and the nuances of special needs planning. The Retirement Trust must incorporate special needs provisions to ensure that program eligibility is not jeopardized. Bear in mind that a Retirement Trust does not take the place of a typical special needs trust – the latter must also be incorporated for non-retirement account assets.

Blogs

EPLO Blogs for You

Have you checked out the EPLO website blogs lately? The EPLO attorneys post timely and informative blogs every few weeks. These are quick and easily read updates that impact you and your estate planning.

- Did you know that women reportedly face much higher rates for long-term care insurance in 2014? If you are a woman who is considering purchasing a LTC insurance plan, you might consider purchasing coverage this year.
- EPLO's Asset Protections blog series addresses the crucial components of a business owner's estate plan, the role of trusts in asset protection planning, and protecting and preserving your assets from third parties.
- The Massachusetts Uniform Trust Code (MUTC) was passed last year. The changes are relevant for those who have trusts as part of their estate plans.

Take a few minutes and check out our blogs. You'll find they are valuable - and needed - information. www.estatepreservationlaw.com/blog/

Spotlight on The Retirement Trust

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I already have a Will and Living (Revocable) Trust. Will the Retirement Trust replace my existing plan?
No – the Retirement Trust does not affect your existing estate plan, it becomes an additional component to your plan. The Retirement Trust is simply a "stand-by" trust that exists to receive the balance of your retirement account after your death (or if you are married, after the death of your spouse if he/she survives you). Your will and other trust(s) will remain in effect to deal with your non-retirement assets.

Will the Retirement Trust "own" my retirement accounts during my life?
No – you will continue to own your retirement accounts during your life. The Retirement Trust will be named as the beneficiary of the accounts upon your death.

How do I name a Retirement Trust as the beneficiary of my retirement accounts?
The Retirement Trust would be named on the beneficiary designation form for each retirement account. Since the designation requires custom language (and often times a separate attachment), we recommend that an attorney assist in this process. At EPLO, we complete these forms for our clients at no cost as part of the process of establishing a Retirement Trust.

Our financial advisor recommended that my spouse and I name each other as the primary beneficiary of our retirement accounts. Would that still be the case if we established Retirement Trusts?
Because of the substantial income tax benefits of the "spousal rollover" option for surviving spouses (to continue deferring required minimum distributions until age 70 ½), it makes sense in most cases to name spouses as primary beneficiaries. While Retirement Trusts can be used for spouses, in most cases their purpose is to receive the accounts after the death of both spouses for the benefit of the children/grandchildren.

I have three children - one is disabled, and needs a Retirement Trust for his share of my IRA. Is that possible?
Yes – you can choose which of your beneficiaries will have a Retirement Trust for his/her share. The trust itself will be customized to provide for those children/beneficiaries in need of trust protection, and the other beneficiaries can receive their shares of the IRA directly, outside of a trust.

The Attorney's Role

Retirement Accounts: What is the Attorney's Role?

Discussions about retirement plans typically take place with financial advisors. However, most people don't think of this as an issue to discuss with their estate planning attorney – in fact, sometimes the attorney doesn't even know who is named as beneficiary on those accounts.

It is important to understand that your will and trust(s) do not control the beneficiaries of your retirement accounts; those assets have a built-in beneficiary designation that you fill out when you establish the account. If you have had a retirement account with your employer for a number of years, or set up your own IRA, stop right now and try to remember when you last updated your beneficiary designations – or better yet, who is even named! Most people cannot. And yet, since you set up your retirement account(s) you may have gone through a divorce or death of a spouse, gotten (re-)married, had additional children or grandchildren, or substantially changed your will.

Don't assume that your financial advisor knows your estate planning objectives. A financial professional's role is to help you invest appropriately and plan for retirement, but decisions about beneficiaries are legal dispositions that should be handled in conjunction with your estate planning attorney.

At EPLO, we discuss these important "funding" decisions with every client as part of the estate planning process. If you have any questions about your retirement account beneficiaries and how they relate to your estate plan, contact one of our attorneys.