Treasury Regulations Permit Naming Trusts As (Designated) Beneficiaries of Retirement Accounts

A trust can become eligible for designated beneficiary treatment, qualifying as a "see-through" trust where the post-death RMDs are calculated based on the life expectancy of the oldest of the trust's underlying beneficiaries.

In order to be treated as a "see-through trust" and qualify as a designated beneficiary, though, the trust must meet four very specific requirements, as stipulated in Treasury Regulation 1.401(a)(9)-4:

1) **The trust must be a valid trust under state law.** This requirement is rather straightforward – the trust must be legally formed under state law. Generally, this just means the trust is not a handwritten trust (not permitted in many/most states), has been properly signed and executed as a trust (witnessed, notarized, etc., as required under state law), and does not contain any provisions that would outright invalidate the trust under state law. For virtually any trust drafted by a competent attorney that was legally signed and executed in the first place, this requirement should be a non-issue.

2) **The trust must be irrevocable, or by its terms become irrevocable upon the death of the original IRA owner.** A revocable living trust that becomes irrevocable upon the death of the owner should qualify under this provision, as would any irrevocable trust that was simply drafted to be irrevocable from the moment it was executed. Notably, while the rules do require that the trust beneficiary be irrevocable (or become so upon death), IRA beneficiary designations themselves remain revocable until death, which means even if an "irrevocable" trust is made as beneficiary of the IRA now, the IRA owner can still "change" the trust by simply creating a new irrevocable trust and changing the beneficiary designation from the "old" irrevocable trust to the "new" irrevocable trust (or alternatively, just get rid of the irrevocable trust altogether if desired). Make sure the trust is properly executed to be a valid trust though (see #1 above), and be cautious about certain joint revocable trusts that may still remain revocable after the *first* death. Bear in mind that the IRA beneficiary "irrevocable" trust could still be a subsection of another trust that is revocable (as long as the particular sections guiding the trust-as-IRA-beneficiary cannot be revoked after death of the IRA owner), and that the trust could also be a testamentary trust created under a Will that doesn't even come into existence as an (irrevocable) trust until the death of the IRA owner.

3) **The trust's underlying beneficiaries must [all] be identifiable as being eligible to be designated beneficiaries themselves.** Treasury Regulations require that if distributions are going to be stretched over the life expectancy of trust beneficiaries, that the trust beneficiaries must be identifiable in the first place, which generally means they should either be identified by name, or identified as members of a "class" of beneficiaries that could be identifiable when the time comes (e.g., "my children" or "my grandchildren" would be fine, but "whoever my trustee decides to make distributions to" would not). Notably, embedded in this requirement that all beneficiaries be identified is that they be identifiable *as designated beneficiaries*, which means they must be individual, living, breathing human beings as beneficiaries; if a charity or some other non-living entity is a trust beneficiary, then the trust will not be

able to do a stretch over the life expectancy of the underlying beneficiaries because not all the underlying beneficiaries as designated beneficiaries *with* a life expectancy.

4) **A copy of "trust documentation" must be provided to the IRA custodian by October 31st of the year following the year of the IRA owner's death.** Under supporting Treasury Regulation 1.401(a)(9), the "documentation" requirement stipulates that the IRA custodian must be provided with either a final list of all trust beneficiaries as of the September-30th-of-year-after-death beneficiary determination date (including contingent and remainder beneficiaries and the conditions under which they would be entitled to payments) along with a certification by the trustee that all of the requirements for stretch distribution are met under the trust, or the trustee can simply provide a copy of the actual (irrevocable) trust document itself to the IRA custodian. Notably, while this is a purely administrative requirement, it *is* a requirement and does have a concrete deadline of October 31st of the year after death that must not be missed.

If the four requirements listed above are met, a trust as IRA beneficiary can qualify as a designated beneficiary, and the post-death RMDs can be stretched, with the caveat that the stretch will still be calculated based upon the life expectancy of the *oldest* trust beneficiary of the trust (who would have the shortest life expectancy).

Naming A Conduit vs Accumulation "See-Through" Trust

While the four requirements for qualifying a trust as a designated beneficiary eligible for "see-through" trust treatment are relatively straightforward, and allow the trust to stretch distributions based on the life expectancy of the oldest underlying trust beneficiary, the complication that arises is determining *which* beneficiaries should be considered on the list to determine who is the oldest in the first place.

Some situations are rather simple. If money is held in trust for the benefit of a spouse and she is the only beneficiary of the trust, then her life expectancy will be used. If the IRA assets will be held in trust for the beneficiary of the spouse but limiting her access to the funds, such that there will be a remainder that goes to the children, the situation is still fairly simple: there are now both current (income) and remainder beneficiaries, but the spouse as parent will clearly be older than the children, so the spouse is still easily determined to be the oldest beneficiary of the trust for purposes of determining the stretch.

For trusts that will hold property in trust – including, perhaps, the trust's interest in a decedent's IRA – for an extended period of time, though, the situation gets more complicated. For instance, if the funds are held in trust where the spouse gets only the income at the optional discretion of the trustee, then when the spouse dies the money continues to be held for the children where they still only get income at the trustee's discretion (and principal remains in place), and then only after the children pass away do the funds go outright to the grandchildren, *and* if there are no (remaining) grandchildren when the children pass away then the funds go to the decedent's alma mater as the "taker of last resort" (the beneficiary if *everyone* else is deceased), the situation is less clear. Should only the spouse be included? Or spouse and children? Or spouse and children and grandchildren? Or spouse, children, grandchildren, and the decedent's alma mater? The distinction matters, because if the alma mater is included, as a charity it is not a designated beneficiary and could render the *entire* stretch IRA invalid (as requirement #3 above was that the trust have only identifiable individual beneficiaries who would themselves be eligible for stretch treatment as a designated beneficiary, and a charity doesn't count!).

To simplify this situation, Treasury Regulation 1.401(a)(9)-5, allows that if the trust requires that all required minimum distributions collected from the IRA will pass through directly and immediately to the underlying income beneficiary, that *only* the income beneficiary's life expectancy must be considered. This "conduit trust" rule essentially permits all other subsequent remainder beneficiaries to be ignored in the process of determining the oldest life expectancy, in exchange for the fact that the trust will not be able to accumulate any of the IRA's RMDs for those subsequent beneficiaries (since they all must pass through immediately each year to the income beneficiary for conduit trust treatment).

By contrast, any trust that *can* accumulate the RMDs as they leave the IRA, and might not subsequently pass them through to the underlying beneficiaries until some later date, is deemed an "accumulation" trust where both the current income *and* remainder beneficiaries must be considered. And in fact, as long as the trust can continue to accumulate RMDs (because there's not yet any outright distribution), it's necessary to continue down the line of trust beneficiaries until the point *is* reached where an outright distribution occurs.

Once the outright distribution is scheduled to occur, no subsequent beneficiaries must be considered for life expectancy purposes under Treasury Regulation 1.401(a)(9)-5, because at that point any future beneficiaries would not actually have a legal right unto themselves but would simply be "mere successors" to the actual stretch beneficiaries. Thus, in the context of the earlier example, the alma mater would not need to be considered as a beneficiary, even under the accumulation trust rules, because the outright distribution was to the grandchildren and so the charitable institution further down the line is considered a mere successor interest to the grandchildren and not a beneficiary unto itself.