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Decision Tree for Naming Retirement Account Beneficiaries after the SECURE Act

The SECURE Act of 2019 is the most impactful legislation affecting retirement accounts in decades. Although the new law includes many positive changes, it no longer permits most non-spouse beneficiaries to withdraw an inherited retirement account over the beneficiary's life expectancy (aka "stretch IRA"). Instead the default rule now requires the entire account to be withdrawn and liquidated by the end of the 10th year after the death of the account owner ("10-year liquidation rule"). This change has major implications for estate planning.

The 10-year liquidation rule results in the acceleration of income tax due, possibly causing beneficiaries to be bumped into a higher income tax bracket and receiving less of the funds contained in the retirement account than under the prior law. However, the SECURE Act does provide a few exceptions to the usual rule that are available to surviving spouses, beneficiaries less than 10 years younger than the account owner, minor children, and disabled individuals. But these exceptions only complicate the estate planning process because your estate planning objectives likely include more than just tax considerations. For example, you might be concerned with protecting a beneficiary's inheritance from future creditors and ex-spouses or preventing your spouse from disinherit your children upon the spouse's remarriage. All these issues should be considered simultaneously when choosing who to name as beneficiaries of your retirement account and whether to integrate trust provisions into the beneficiary designation.

The purpose of this article is to provide a structured analysis; i.e., a decision tree; for determining whether to name a trust as beneficiary of a retirement account.

A summary is included at the end of the article.

Part One: Spouse Beneficiary

If you are married, you should name your spouse as primary beneficiary of your tax-deferred retirement account unless you have identified a reason not to. Upon your death your surviving spouse would have two choices: (1) move the assets from your account into his or her own IRA (aka "rollover IRA"), or (2) elect inherited IRA treatment and withdraw annually at least the required minimum distributions over his or her remaining life expectancy (aka "stretch IRA"). The usual 10-year liquidation rule does not apply.

A rollover IRA is usually a better choice for income tax optimization because: (1) it requires no distributions to a surviving spouse under age 72, and (2) it permits the use of a more favorable tax table when calculating the required minimum distributions to a surviving spouse after attaining age 72. A rollover IRA may also offer more creditor protection because the alternative – an inherited IRA – is exposed to creditors in most states (but not for Arizona residents).

But you should consider naming a trust as beneficiary if either of the following concerns is paramount:

1. Prevent Spouse from Making Changes. If you want to prevent your spouse from disinherit your children or other preferred remainder beneficiaries after your death, which often occurs when family dynamics are disrupted, or your spouse chooses to remarry.
2. Protect from a Clear and Present Danger Related to Your Spouse. If you want to protect your retirement account from a clear and present danger related to your spouse, such as concerns about your spouse's spendthrift habits, susceptibility to undue influence, or qualification for government-sponsored health benefits.

If YES, then you must consider what type of trust to name as beneficiary. There are 3 options: 1- Conduit Trust, 2- Accumulation Trust, 3- Charitable Remainder Trust.

Option #1 Conduit Trust (favors income tax optimization)

How it Works:

If you prefer using a trust that favors income tax optimization, then you should consider naming a conduit trust as beneficiary. A conduit trust will pay out required minimum distributions from the retirement account to your spouse over his or her remaining life expectancy. The conduit trust qualifies for stretch IRA treatment during your spouse's lifetime, which exempts the trust from the usual 10-year liquidation rule applicable to inherited retirement accounts payable to trusts. The trust document may, but need not, permit additional distributions in the discretion of a third-party trustee. Unless the account is Roth-qualified, all distributions will be taxable at your spouse's income tax rate.

How to Implement:

A conduit trust may be integrated into a separate property revocable living trust holding other separate assets, if you have one. However, an alternative is to prepare a stand-alone IRA beneficiary trust solely for the purpose of serving as primary beneficiary of your retirement account. This approach is more likely to achieve quick acceptance by the account custodian's legal department. Also, a stand-alone IRA beneficiary trust is always the preferred option if the contingent beneficiaries of your retirement account are different than the contingent beneficiaries for your other assets.

Analysis:

Because the conduit provisions require distributions equal to what would be required without a trust involved, the only reason to choose this option is if you want to name a third-party trustee to manage the investments and/or restrict additional withdrawals over the required minimum amounts. Even then a “trusteed IRA” managed by the account custodian, if offered, may be a simpler option than naming a trust as beneficiary.

Option #2 Accumulation Trust (favors asset protection)

How it Works:

If you prefer using a trust with robust asset protection features, then you should consider naming an accumulation trust as beneficiary. An accumulation trust is subject to the usual 10-year liquidation rule, but the assets distributed to the trust may be held (accumulated) within the trust. This option gives a third-party trustee full control over the timing of distributions from the account to the trust (during the 10-year liquidation period) and distributions from the trust to your spouse (at any time pursuant to the provisions of the trust document). The accumulated trust assets remain protected from outside threats that might arise against your spouse and other beneficiaries. Unless the account is Roth-qualified, all withdrawals will be taxable either (A) to the trust at the trust’s income tax rate, if accumulated in the trust, or (B) to your spouse at his or her income tax rate, if distributed to your spouse.

How to Implement:

An accumulation trust may be integrated into a separate property revocable living trust holding other separate assets, if you have one. However, an alternative is to prepare a stand-alone IRA beneficiary trust solely for the purpose of serving as primary beneficiary of your retirement account. This approach is more likely to achieve quick acceptance by the account custodian’s legal department. Also, a stand-alone IRA beneficiary trust is always the preferred option if the contingent beneficiaries of your retirement account are different than the contingent beneficiaries for your other assets.

Analysis:

The accumulation trust will ensure that any remaining assets in the retirement account and trust upon your spouse’s death (or remarriage, if desired) are distributed to your preferred beneficiaries (e.g., your children). Your spouse will not be able to redirect assets from your retirement account or the trust to other beneficiaries you did not approve. Also, the accumulated trust assets are shielded from creditors of your spouse, future spouses of your spouse, or anyone else who might want to swipe the inheritance.

While it is permissible to name your spouse as trustee of an accumulation trust, doing so rarely makes sense because it conflicts with the primary objective of an accumulation trust (i.e., asset protection).

Option #3 Charitable Remainder Trust (balances both objectives)

How it Works:

If you desire a trust with robust asset protection features without sacrificing income tax optimization, then you should consider naming a charitable remainder trust as beneficiary. A charitable remainder trust will establish a predictable plan for the timing and amount of distributions to your spouse by using an annuitized income stream or “unitrust” percentage. This approach balances the short-term objective of providing for your spouse and the long-term objective of providing for your preferred contingent beneficiaries (e.g., your children).

Upon your death your trustee (who may be your spouse, if desired) must liquidate your retirement account immediately, but the entire amount will pass income-tax free to the trust. Each subsequent year the trustee is required to distribute an established amount (“annuity”) or a percentage of trust assets (“unitrust”) to your spouse for his or her lifetime, all of which are subject to income tax. Meanwhile, the balance of trust assets may continue to be invested in a tax-deferred environment. Upon your spouse’s death the annuity or unitrust amount will continue to be distributed to your preferred beneficiaries (e.g., your children) for a term of years or until the death of the last remaining beneficiary. When the distribution period ends, any remaining trust assets are distributed to the charity you named in the trust originally, although you may include a provision giving beneficiaries the right to name a different charity as remainder beneficiary.

How to Implement:

The charitable remainder trust provisions can be integrated into a will or revocable living trust, if you have one, then followed by naming the charitable remainder trust as beneficiary of your retirement account. However, an alternative is to prepare a stand-alone charitable remainder trust solely for the purpose of serving as primary beneficiary of your retirement account. This approach is more likely to achieve quick acceptance by the account custodian’s legal department. Also, a stand-alone IRA beneficiary trust is always the preferred option if the contingent beneficiaries of your retirement account are different than the contingent beneficiaries for your other assets.

Analysis:

A unique feature of the charitable remainder trust is that it provides an orderly, predictable plan for the timing and amount of distributions to your spouse. This is not necessarily the case for conduit and accumulation trusts.

The charitable remainder trust ensures that any remaining assets in the trust upon your spouse's death are payable to your preferred beneficiaries (e.g., your children). Your spouse will not be able to redirect assets from your retirement account or the trust to other beneficiaries you did not approve. Also, the accumulated trust assets are shielded from creditors of your spouse, future spouses of your spouse, or anyone else who might want to swipe the inheritance.

Using a charitable remainder trust also provides income tax optimization because it mimics the highly favorable stretch IRA treatment that is available when naming a surviving spouse as primary beneficiary. Only distributions from the trust are subject to income tax and they can be made over a much longer period than 10 years. The distributions may also benefit from favorable capital gains tax treatment in later years. Also, the trust can double as a credit shelter trust because it is not subject to estate tax at the surviving spouse's death.

There is one catch, however. The present value of the charitable remainder interest must be at least 10% of the retirement account in order to qualify under IRS rules. What this really means is that you need to be charitably inclined at least to a measurable amount because a charity will likely inherit a portion of the trust. If this bothers you, but you still want to use a charitable remainder trust, then consider buying life insurance to replace the projected remainder distribution to charity.

Part Two: Non-Spouse Beneficiaries

By default, you should list the names of your children or other preferred beneficiaries as beneficiaries on the standard beneficiary designation form unless you have identified a reason not to. In most cases, a beneficiary must liquidate his or her share of your retirement account by the end of the 10th year following your death in whatever increments he or she chooses. This is the default law, but there are exceptions. A minor child qualifies for stretch IRA treatment and need take only required minimum distributions until age 18 or possibly until age 26 if the child remains a student until then. Also, a disabled or chronically ill beneficiary, or any individual beneficiary less than 10 years younger than you, qualifies for stretch IRA treatment and need take only required minimum distributions during the beneficiary's lifetime. Withdrawals will be subject to income tax unless taken from a Roth-qualified account.

But you should consider naming a trust as beneficiary if one of the following estate planning objectives is paramount:

1. Delay Inheritance Until Young Child is Ready to Inherit. If you want to delay a young child's unfettered access to your retirement account until an age higher than 18.
2. Restrict Inheritance in Response to an Identifiable Clear and Present Danger. If you want to restrict access to your retirement account in response to an identifiable clear and present danger related to your beneficiary, such as concerns about your beneficiary's spendthrift habits, susceptibility to undue influence, or qualification for government-sponsored health benefits.
3. Protect Inheritance from Future Threats. If you want to protect your retirement account from future threats that might arise against a beneficiary, even for responsible adult beneficiaries. These future threats might include judgment creditors, ex-spouses, debt collectors, and other predators who might want to swipe the inheritance.

If YES, then you must choose what type of trust to name as beneficiary. There are 3 possible choices: 1- Conduit Trust, 2- Accumulation Trust, 3- Charitable Remainder Trust. Your best option depends on what your primary objective is regarding how to distribute your retirement account to your beneficiaries.

Objective 1- Delay Inheritance for Young Child

Under the SECURE Act, when a minor child inherits a retirement account, the minor child's custodian (under UTMA rules) or conservator (under court supervision) may elect stretch IRA treatment on behalf of the minor. A required minimum distribution would need to be made from the account annually until the minor attains the age of majority. In Arizona, this is 18 years of age; however, a child may still qualify as a minor until age 26 if he or she remains a student during that time. Upon attaining age 18 (or possibly age 26), the usual 10-year liquidation rule goes into effect.

It should be emphasized that although a minor child qualifies for an exception to the usual 10-year liquidation rule, nothing would prevent the child from liquidating the entire account at any time after attaining age 18 if you rely on a custodianship or a court-appointed conservatorship until then. The stretch IRA treatment is an *option* available to the child (or more accurately, the child's custodian or conservator) until the child attains age 18 (or possibly age 26), not a *restriction*. The child may fully withdraw the account at any time after the restrictions imposed by the custodianship or conservatorship end. If you are uncomfortable with this possibility, then you must consider whether the value of your retirement account is enough to justify the added complexity of naming a trust as beneficiary. For accounts with less than \$10,000 per beneficiary, it makes no sense to name a trust as beneficiary (at least when the beneficiary lives in Arizona). Also, for accounts with less than about \$100,000 per beneficiary, it still may be reasonable to rely on a custodianship or conservatorship for a young beneficiary because the distributions would be relatively small.

For accounts with more than about \$100,000 per beneficiary, you should consider naming a trust as beneficiary because it will allow you to raise the minimum age a beneficiary must attain in order to liquidate the inherited retirement account. When delaying inheritance for a young child is a paramount concern there are 2 choices for types of trusts to choose from:

Option #1 Conduit trust (favors income tax optimization)

How it Works:

If you prefer using a trust that favors income tax optimization, then you should consider naming a conduit trust as beneficiary. A conduit trust will pay out required minimum distributions from the retirement account to your beneficiary until the beneficiary attains age 18 (or possibly age 26 if a student). The conduit trust qualifies for "stretch IRA" treatment during this period, which exempts the trust from the usual 10-year liquidation rule applicable to inherited retirement accounts payable to trusts. The trust document may, but need not, permit additional distributions in the discretion of a third-party trustee. Unless the account is Roth-qualified, all distributions will be taxable at your beneficiary's income tax rate. Upon attaining age 18 (or possibly age 26 if a student) the usual 10-year liquidation rule goes into effect. Any withdrawals from the account must be distributed outright to the beneficiary.

How to Implement:

Conduit trust provisions may be integrated into your revocable living trust, if you have one, or into a testamentary trust described in your will. However, both require the second step of specifically naming the trust as beneficiary using the retirement account custodian's beneficiary designation form (either online or on paper). If you have a living trust-based estate plan, then you would just use the name and date of the living trust. If using a will-based estate plan, then it is important to specifically refer to the testamentary trust described in the will.

However, an alternative is to prepare a stand-alone IRA beneficiary trust solely for the purpose of serving as beneficiary of your retirement account. This approach is more likely to achieve quick acceptance by the account custodian's legal department. Also, a stand-alone IRA beneficiary trust is always the preferred option if the beneficiaries of your retirement account are different than the beneficiaries for your other assets.

Analysis:

Because the conduit provisions require distributions equal to what would be required without the trust involved, the only reason to choose this option is if you want to name a third-party trustee to manage the investments and/or restrict additional withdrawals over the required minimum amounts. Even then a "trusteed IRA" managed by the account custodian, if offered, may be a simpler option than naming a trust as beneficiary.

The conduit trust will end no later than 10 years after the beneficiary attains the age of majority; no exceptions. In other words, this type of trust favors income tax optimization and disfavors asset protection.

Option #2 Accumulation trust (favors asset protection)

How it Works:

If you prefer using a trust with robust asset protection features, then you should consider naming an accumulation trust as beneficiary. An accumulation trust is subject to the usual 10-year liquidation rule, but the assets distributed to the trust may be held (accumulated) within the trust. This option gives a third-party trustee more control over the timing of distributions from the account to the trust (during the 10-year liquidation period) and distributions from the trust to your beneficiary (at any time pursuant to the provisions of the trust document). The accumulated trust assets remain safely in the trust until the trustee chooses to make a distribution. Unless the account is Roth-qualified, all withdrawals will be taxable either (A) to the trust at the trust's income tax rate, if accumulated in the trust, or (B) to your beneficiary at his or her income tax rate, if distributed to your beneficiary.

How to Implement:

An accumulation trust may be integrated into your revocable living trust, if you have one, or into a testamentary trust described in your will. However, both require the second step of specifically naming the trust as beneficiary using the retirement account custodian's beneficiary designation form (either online or on paper). If using a living trust-based estate plan, then you would just use the name and date of the living trust. If using a will-based estate plan, then it is important to specifically refer to the testamentary trust described in the will. However, an alternative is to prepare a stand-alone IRA beneficiary trust solely

for the purpose of serving as beneficiary of your retirement account. This approach is more likely to achieve quick acceptance by the account custodian's legal department. Also, a stand-alone IRA beneficiary trust is always the preferred option if the beneficiaries of your retirement account are different than the beneficiaries for your other assets.

Analysis:

At first glance the accumulation trust seems inferior to the conduit trust because it must use the 10-year liquidation rule instead of qualifying for stretch IRA treatment, even when the beneficiary is a young child. But while a conduit trust requires the withdrawn amounts to be distributed immediately to the beneficiary, an accumulation trust allows the trustee to retain any withdrawn amounts in trust. In fact, no distributions to the young beneficiary are required at all. Thus, an accumulation trust integrates asset protection features for the entire duration of the trust as you choose to define it. This is different than the conduit trust, which mandates distributions to the beneficiary and must be fully liquidated within 10 years after the beneficiary attains the age of majority. Certainly, this difference can be quite meaningful if the value of the retirement account is substantial.

Also, the accumulation trust works best if your estate plan calls for a common trust until your youngest child attains a specified age and you want to give the trustee full discretion to allocate the assets from your retirement account among any of your children as the trustee deems best under the circumstances.

Another technical issue is that beneficiaries of an accumulation trust may only redirect the remaining retirement account assets to individuals, not charities, in the event the beneficiary dies while the trust still exists. Without this restriction, the accumulation trust must use an even less tax favorable 5-year liquidation rule.

Objective 2- Restrict Inheritance in Response to Danger

You may have identified a clear and present danger that calls for the restriction of a beneficiary's inheritance. Examples include beneficiaries who (1) are presently eligible for needs-based government benefits, (2) have spendthrift or gambling habits, (3) are going through a divorce or very well might, (4) have major creditor problems such as a recent bankruptcy, or (5) have an outstanding judgment resulting from a lawsuit or past due debt, or (6) might be susceptible to undue influence by others.

In this case it makes little sense to name a conduit trust as beneficiary because it would require all withdrawals from the retirement account to be distributed immediately to the beneficiary. There may be a few scenarios under this objective where using a conduit trust or charitable remainder trust still remain feasible options, but those scenarios carry the risk that mandatory withdrawals (or annuity or unitrust payments in the case of a CRT) must

be distributed outright to the beneficiary. It is assumed, therefore, that you would use an accumulation trust and name a third-party trustee in order to enforce whatever restrictions are identified in the trust document.

Option #1 Accumulation trust (this is primary trust option)

How it Works:

If restricting inheritance from a clear and present danger is your primary objective, then you should consider naming an accumulation trust as beneficiary unless the value of the account is so small as not to justify it. An accumulation trust is subject to the usual 10-year liquidation rule, but the assets distributed to the trust may be held (accumulated) within the trust. This option gives a third-party trustee full control over the timing of both distributions from the account to the trust (during the 10-year liquidation period) and distributions from the trust to your beneficiary (at any time pursuant to the provisions of the trust document). The accumulated trust assets remain safely in the trust until the trustee chooses to make a distribution. Unless the account is Roth-qualified, all withdrawals will be taxable either (A) to the trust at the trust's income tax rate, if accumulated in the trust, or (B) to your beneficiary at his or her income tax rate, if distributed to your beneficiary.

How to Implement:

An accumulation trust may be integrated into your revocable living trust, if you have one, or into a testamentary trust described in your will. However, both require the second step of specifically naming the trust as beneficiary using the retirement account custodian's beneficiary designation form (either online or on paper). If using a living trust-based estate plan, then you would just use the name and date of the living trust. If using a will-based estate plan, then it is important to specifically refer to the testamentary trust described in the will. However, an alternative is to prepare a stand-alone IRA beneficiary trust solely for the purpose of serving as beneficiary of your retirement account. This approach is more likely to achieve quick acceptance by the account custodian's legal department. Also, a stand-alone IRA beneficiary trust is always the preferred option if the beneficiaries of your retirement account are different than the beneficiaries for your other assets.

Analysis:

Because this scenario assumes the existence of an identifiable clear and present danger, it rarely makes sense for the beneficiary to serve as trustee of the trust. In some cases, such as when the beneficiary has special needs, the beneficiary may even be ineligible to serve as trustee. However, the trust can be drafted to permit the beneficiary to remove and replace the third-party trustee, if desired.

Another technical issue is that beneficiaries of an accumulation trust may only redirect the remaining retirement account assets to individuals, not charities, in the event the beneficiary dies while the trust still exists. Without this restriction, the accumulation trust must use an even less tax favorable 5-year liquidation rule or the so-called “ghost life expectancy” rule, both of which are likely to be shorter in duration than the 10-year liquidation rule.

Objective 3- Protect Inheritance from Future Threats

If your primary objective is the protection of a beneficiary’s inheritance from future threats that do not exist currently, then it makes no sense to name a conduit trust as beneficiary because the distribution rules are precisely the same whether naming a trust as beneficiary or just naming the individual as beneficiary. In theory, a third-party trustee could be named to manage the account, but the assumption here is that the individual is an adult responsible beneficiary who is willing and able to manage the inheritance.

For accounts with less than \$100,000 per beneficiary, it makes little sense to name a trust as beneficiary because the amount is relatively small and inherited IRAs are protected by law for Arizona residents. But for accounts with more than \$100,000 per beneficiary, you should consider naming a trust as beneficiary because it will allow the beneficiary to protect the inheritance from future threats (e.g., judgment creditors, ex-spouses, debt collectors, and other predators who might want to swipe the inheritance). When protecting inheritance from future threats against a beneficiary is a paramount concern there are 2 choices for types of trusts to choose from:

Option #1 Accumulation trust (favors asset protection)

How it Works:

If you prefer using a trust with robust asset protection features, then you should consider naming an accumulation trust as beneficiary. An accumulation trust is subject to the usual 10-year liquidation rule, but the assets distributed to the trust may be held (accumulated) within the trust. This option gives the trustee (who may also be the beneficiary) full control over the timing of distributions from the account to the trust (during the 10-year liquidation period) and distributions from the trust to your beneficiary (at any time pursuant to the provisions of the trust document). The accumulated trust assets remain safely in the trust until the trustee chooses to make a distribution. Unless the account is Roth-qualified, all withdrawals will be taxable either (A) to the trust at the trust’s income tax rate, if accumulated in the trust, or (B) to your beneficiary at his or her income tax rate, if distributed to your beneficiary.

How to Implement:

An accumulation trust may be integrated into your revocable living trust, if you have one, or into a testamentary trust described in your will. However, both

require the second step of specifically naming the trust as beneficiary using the retirement account custodian's beneficiary designation form (either online or on paper). If using a living trust-based estate plan, then you would just use the name and date of the living trust. If using a will-based estate plan, then it is important to specifically refer to the testamentary trust described in the will. However, an alternative is to prepare a stand-alone IRA beneficiary trust solely for the purpose of serving as beneficiary of your retirement accounts. This approach is more likely to achieve quick acceptance by the account custodian's legal department. Also, a stand-alone IRA beneficiary trust is always the preferred option if the beneficiaries of your retirement account are different than the beneficiaries for your other assets.

Analysis:

The accumulated trust assets are shielded from creditors of your beneficiary, future spouses of your beneficiary, or anyone else who might want to swipe the inheritance.

Because this scenario assumes the beneficiary is a responsible adult, it makes sense to name the beneficiary as sole trustee of the trust. However, the trust should be drafted to permit the trustee to resign and name an independent trustee instead because this enhances the level of protection if an actual threat arises.

Another technical issue is that beneficiaries of an accumulation trust may only redirect the remaining retirement account assets to individuals, not charities, in the event the beneficiary dies while the trust still exists. Without this restriction, the accumulation trust must use an even less tax favorable 5-year liquidation rule or the so-called "ghost life expectancy" rule, both of which are likely to be shorter in duration than the 10-year liquidation rule.

Option #2 Charitable Remainder Trust (adds income tax optimization)

How it Works:

If you want a trust with robust asset protection features without sacrificing income tax optimization, then you should consider naming a charitable remainder trust as beneficiary. This approach uses trust laws to shield inherited assets from future threats, while using the tax-favored charitable trust provisions to achieve income tax optimization. A charitable remainder trust will establish a predictable plan for the timing and amount of distributions to your beneficiary by using an annuitized income stream or "unitrust" percentage.

Upon your death your trustee (who may be your beneficiary, if desired) must liquidate your retirement account immediately, but the entire amount will pass income-tax free to the trust. Each subsequent year the trustee is required to distribute an established amount ("annuity") or percentage of trust assets

(“unitrust”) to your beneficiaries (e.g., your children) for a term of years or until the death of the last remaining beneficiary, all of which are subject to income tax. Meanwhile, the balance of trust assets may continue to be invested in a tax-deferred environment. When the distribution period ends, any remaining trust assets are distributed to the charity you named in the trust originally, although you may include a provision giving beneficiaries the right to name a different charity as remainder beneficiary.

How to Implement:

The charitable remainder trust provisions can be integrated into a will or revocable living trust, if you have one, then followed by naming the charitable remainder trust as beneficiary of your retirement account. However, an alternative is to prepare a stand-alone charitable remainder trust solely for the purpose of serving as beneficiary of your retirement accounts. This approach is more likely to achieve quick acceptance by the account custodian’s legal department. Also, a stand-alone IRA beneficiary trust is always the preferred option if the contingent beneficiaries of your retirement account are different than the contingent beneficiaries for your other assets.

Analysis:

A unique feature of the charitable remainder trust is that it provides an orderly, predictable plan for the timing and amount of distributions to your beneficiaries. This is not necessarily the case for conduit and accumulation trusts.

The charitable remainder trust assets are shielded from creditors of your beneficiary, future spouses of your beneficiary, or anyone else who might want to swipe the inheritance.

Using a charitable remainder trust also provides income tax optimization because it mimics the highly favorable stretch IRA treatment that is not usually available to a non-spouse beneficiary. Only distributions from the trust are subject to income tax and they can be made over a much longer period than 10 years. The distributions may also benefit from favorable capital gains tax treatment in later years.

There is one catch, however. The present value of the charitable remainder interest must be at least 10% of the retirement account in order to qualify under IRS rules. What this really means is that you need to be charitably inclined at least to a measurable amount because a charity will likely inherit a portion of the trust. If this bothers you, but you still want to use a charitable remainder trust, then consider buying life insurance to replace the projected remainder distribution to charity.

Summary of Decision Tree for Naming Retirement Account Beneficiaries after the SECURE Act

Summary for Spouse Beneficiary:

If married, name your spouse as primary beneficiary of your retirement account *unless* (1) you want to prevent your spouse from dis inheriting your children or other preferred remainder beneficiaries after your death, which often occurs when family dynamics are disrupted, or your spouse chooses to remarry; or (2) you need to protect the account from a clear and present danger related to your spouse, such as concerns about your spouse's spendthrift habits, susceptibility to undue influence, or qualification for government-sponsored health benefits.

If one of the above-described exceptions applies, then choose a type of trust to name as beneficiary:

1. **Conduit** (favors income tax optimization, qualifies for stretch IRA treatment, all withdrawals pass through to spouse, trustee may not accumulate assets in trust, only makes sense if you name a third-party trustee)
2. **Accumulation** (favors asset protection, subject to usual 10-year liquidation rule, trustee may accumulate withdrawals from account or pass them through to beneficiary, only makes sense if you name a third-party trustee)
3. **Charitable remainder** (balances both income tax optimization and asset protection, trust assets remain in tax-deferred environment until distributed, trust pays out annuity or percentage amount to spouse for life then to contingent beneficiaries for term of years or life, balance to charity when distribution period ends, spouse may serve as trustee)

Summary for Non-Spouse Beneficiaries:

When naming non-spouse beneficiaries, you should first determine your primary objective regarding how to distribute the retirement account to your beneficiaries:

1. Give outright (no desire to delay, restrict, or protect)
2. Delay for young child
3. Restrict in response to an identifiable clear and present danger
4. Protect from future threats (lawsuits, ex-spouse, debt collectors, etc.)

If **GIVE OUTRIGHT**, then list the beneficiary names on the standard beneficiary designation form.

If **DELAY** and account value is more than \$100,000 per beneficiary, then name a type of trust as beneficiary instead:

1. **Conduit** (favors income tax optimization, qualifies for stretch IRA treatment until beneficiary attains age of majority then usual 10-year liquidation rule goes into effect, all withdrawals pass through to beneficiary, trustee may not accumulate asset in trust, requires third-party trustee)
2. **Accumulation** (favors asset protection, subject to usual 10-year liquidation rule, trustee may accumulate withdrawals from account or pass them through to beneficiary, no distributions required, requires third-party trustee until a specified age)

If **RESTRICT**, then choose an **Accumulation** trust to name as beneficiary (same as accumulation trusts above and below, except beneficiary is ineligible to serve as trustee in most scenarios). Conduit and charitable remainder trusts might be feasible, but both require mandatory distributions that would not be restricted.

If **PROTECT** and account value is more than \$100,000 per beneficiary, then choose a type of trust as beneficiary instead:

1. **Accumulation** (favors asset protection, subject to usual 10-year liquidation rule, trustee may accumulate withdrawals from account or pass them through to beneficiary, no distributions required, beneficiary may serve as trustee)
2. **Charitable remainder** (adds income tax optimization, trust assets remain in tax-deferred environment until distributed, trust pays out annuity or percentage amount to beneficiaries for a term of years or life, balance to charity when distribution period ends, beneficiary may serve as trustee)