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Guide...Protect...Preserve

Avoid These 6 Mistakes In Stretch IRA Planning

As talk of the possibility of tax reform continues in Washington, there's an increased focus on the rules for "stretch IRAs." This retirement planning technique, which enables you to preserve assets in an inherited IRA for an extended period, could be could be targeted in a larger tax reform package. For the time being, however, stretch IRA planning remains a viable option for many people.

But to use a stretch IRA successfully, you'll need to follow a number of important rules and avoid common mistakes made by those who inherit IRA assets.

If you own an IRA, you must take required minimum distributions (RMDs) annually beginning the year after you reach age 70½. Otherwise, you'll be hit with a stiff IRS penalty. Those distributions are taxed at your rate for ordinary income—which could be as high as 39.6%—and are based on a calculation that considers the account balance at the end of the previous year and your life expectancy (or your joint life expectancies with your spouse).

However, beneficiaries who inherit your IRA can arrange for RMDs based on their own life own expectancies, unless they choose to empty the account more quickly. Stretching out the IRA in this fashion can help preserve wealth for younger generations.

With those basics in mind, consider these six common mistakes in stretch IRA planning:

Mistake #1: Your account is titled improperly. When someone dies and IRA assets are inherited, it's crucial to ensure that the account name is titled correctly. For example, if someone other than your spouse inherits your IRA, your name should remain on the inherited IRA account title and it must be indicated that it is an inherited IRA by using the words "beneficiary" or "beneficiary IRA" or "inherited IRA."

Mistake #2: You fail to take RMDs. If the IRA account holder already was taking RMDs at the time of death, inheritors will need to make sure that the RMD is withdrawn for the year in which the account holder died. Failing to meet this requirement triggers a penalty equal to 50% of the amount that should have been withdrawn.

Mistake #3: You, as the primary beneficiary, fail to utilize a disclaimer when appropriate. A qualified disclaimer is a legal document that effectively says you choose not to receive the IRA assets, which then will pass to the contingent beneficiaries listed on the IRA paperwork. This

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Tax Reform Outlook: Cloudy, With A Chance Of A Law

Ever since President Trump entered office, the drums have been beating loudly for a major overhaul of the tax system, echoed by support from a Republican-led Congress. So what are the chances for tax reform legislation this year?

In his early days in office, Trump expressed intentions to cut individual tax rates and consolidate other provisions, implement tax breaks to spur business growth, and repeal the federal estate tax, among other proposals. The House GOP issued a blueprint for tax reform in 2016 that seeks many of the same objectives, although by different means in some cases.

It seems at first blush that there's enough sentiment in Washington to pass a comprehensive bill, but there undoubtedly will be unexpected twists and turns along the way. In April, the Trump administration rolled out a revised tax plan emphasizing tax cuts for individuals and businesses. But the prospects for eventual enactment remain unclear.

If passed, such tax legislation likely would affect many aspects of your financial affairs, including investments, retirement plans, IRAs, estates, and trusts.

What should you do now? With uncertainty in the air, the best idea probably is to stick with your current plans and closely monitor the situation. We will be ready to help you if and when the time comes for action.

Mary Jane Callaghan & Mitch Glicksman

When To Disclaim An Inherited IRA

Should you ever pass up a chance to get more money? It depends. Suppose you're in line to inherit IRA assets. When it makes sense, you might use a "qualified disclaimer" so that the assets bypass you on the way to someone else.

A disclaimer is a legal document that lets you waive your right to receive money or property from an estate. If you execute a disclaimer, it's as if you never inherited the assets. Instead, they go directly to the next people in line to receive them. In the case of an IRA, the assets typically wind up with the account's contingent beneficiaries.

Why would you do this? There are two main reasons:

1. Assuming you don't need the money, you might prefer that the assets go directly to the younger generation, usually your own kids or grandkids. You were going to give the assets to them eventually anyway, right? A disclaimer shortens the process while lengthening the time over which the beneficiaries must take required minimum distributions (RMDs) from the account. RMDs are based on the life expectancies of the beneficiaries, so the younger they are, the longer the wealth can be preserved.

2. A disclaimer may reduce a family's overall tax liability. The RMDs from IRAs generally are taxed at ordinary income rates, which go as high as 39.6%. Younger children and grandchildren are likely to pay tax at a much lower rate.

For a disclaimer to work, it has to be an irrevocable, unqualified refusal to accept property, and it must meet the following requirements:

- It must be in writing with a declaration and signature of the person who is making the disclaimer.
- It must identify the property (or the partial interest in the property) that is being disclaimed.
- It must be delivered to the party or entity responsible for transferring the assets (for example, an IRA custodian or trustee).
- The disclaimer has to be executed less than nine months after the property was transferred (or within nine months of when the disclaiming person reaches age 21, if that's sooner).
- As a result of the disclaimer, the assets must pass to the new recipients without any direction from the person making the disclaimer. You can't decide to give the money to someone other than the legal beneficiaries next in line.

This process can be technically complicated, so you'll need to work with an attorney to provide the proper language for a disclaimer, which must take into account whatever is required under state law. Also, take great care in completing any beneficiary designation forms furnished by an institution. ●

What Would Estate Tax Repeal Mean?

If President Trump and the Republican-led Congress get their way, the federal estate tax will be repealed. This could be good news for wealthy families that were facing a hefty estate tax bill in the near future. However, if certain changes accompanying the estate tax repeal also are enacted, other families may encounter an unpleasant income tax surprise.

Normally, an unlimited marital deduction shields transfers between spouses from federal estate and gift taxes, while a separate, finite exemption shelters gifts and bequests to other beneficiaries, including your children. The current exempt amount, which is indexed for inflation, is $5.49 million in 2017. The top tax rate on additional amounts is 40%.

In addition, heirs can benefit from a "step-up" in basis when they inherit investment assets—they're valued on the date of death rather than what was paid for them. So if someone acquired securities for $1 million and it was worth $5 million when that person died, the beneficiary's adjusted basis for income tax purposes is $5 million. The $4 million of appreciation that occurred before the death remains untaxed forever.

Assuming the estate tax is repealed effective for 2017, there would be no more federal estate tax worries for families inheriting an estate worth more than $5.49 million. However, under the latest proposals, Congress also would eliminate the step-up in basis (with an $10 million exception for farms and small business interests), and that could result in income tax problems for many families.

Returning to the example of giving $5 million of assets with a basis of $1 million to non-spouse beneficiaries, no estate tax would be due under the current law, thanks to

Four Tax-Wise Ways To Donate Gifts To Charity

How can you donate to charity? Let us count the ways. Although there are many variations on these themes, there are four basic paths for making contributions to charitable organizations that let you take tax deductions while pursuing your philanthropic goals. They are:

1. Direct contributions: This is the easiest method. You simply write a check or make an online donation. If you're giving tangible property, such as artwork, you'll need to deliver it physically to the charitable group.

Most such contributions are fully deductible on your tax return, but there could be limitations on the size of your write-off based on your adjusted gross income (AGI) for the year:

- Contributions to public charities are limited to 50% of your AGI.
- Contributions of appreciated property (for example, publicly traded stocks) to public charities can't exceed 30% of your AGI.
- Contributions of appreciated property to private foundations are limited to 20% of your AGI.

But in all of these cases any amount that exceeds the limits can be claimed on the following year's return, and such "carryovers" may continue for up to five years.

2. Donor-advised funds: With a donor-advised fund, you give your money to a fund that's set up with an institutional partner. There might be a minimum contribution amount, and the fund may charge fees to cover its costs. But one big advantage of this approach is that you can make a donation to the fund and get an immediate tax deduction and then decide later where you want your money to go.

Once you choose to give a specified amount to a particular charity, the fund will verify that the organization is eligible to receive tax-deductible contributions. Once your grant is approved, the money goes to the group with an indication that it was made on your recommendation. You also can request that your gift be made anonymously.

3. Charitable gift annuities: This approach is somewhat more sophisticated than direct gifts and donor-advised funds. A charitable gift annuity is a contract between a donor and a charity. You agree to transfer money, securities, or other assets to the organization, which in turn agrees to make specified payments to "annuitants"—usually you or you and someone else you designate.

What are the tax consequences? As the donor, you're entitled to a charitable deduction in the year you make your donation to the charity that is adjusted to account for the expected payments you'll receive, based on your life expectancy and other factors.

4. Charitable trusts: There are two main types to consider: the charitable remainder trust (CRT) and the charitable lead trust (CLT).

With a CRT, you set up the trust and transfer selected assets to it. The charity often acts as the trustee and manages the assets. During the trust term, you (or another beneficiary or beneficiaries you specify) receive regular payments from the trust. The CRT may last for a term of specified years or your lifetime. Finally, when the trust ends, the remaining assets from your contribution (the remainder) go to the charity. You get a current tax deduction based on the projected value of that remainder.

A CLT works the opposite way. You still transfer assets to the trust, but annual payments go to the specified charity, and the remainder at the end of the trust term goes to the beneficiaries you designated.

Regardless of whether you use a CRT or a CLT, the annual payments may be based on a fixed amount or a percentage of assets. Other special rules apply, so be sure to obtain expert guidance.

This is a brief overview of current rules. But these approaches could be affected by proposed tax changes. We'll keep you up to date on any changes. ●

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the $5.49 million exemption. But under the proposed reforms (and barring any exemptions), if beneficiaries carry over the basis on those shares and sell the assets for $5 million, they will have a taxable gain of $4 million, subject to the prevailing tax rates for capital gains.

Of course, this is just a hypothetical example and other rules (e.g., a $1 million exemption) could apply, but the potential for major income tax liability is real. Also, state estate taxes may still be a factor. Once it becomes clear whether estate tax reform will be enacted, and what shape it will take, meet with your financial and tax advisors to map out a strategy. ●

Trust As IRA Beneficiary: Not Crazy

You may have heard that you can't name a trust as a beneficiary of your IRA—but in fact that is a perfectly legal option for IRA owners. But whether you should do it is a completely different story and requires further analysis.

IRAs can be complicated enough on their own without bringing a trust into the equation. And if you do name a trust as a beneficiary and then make a mistake with your account, the tax consequences could be devastating—so proceed with extreme caution. You'll need to work with an attorney experienced in these matters.

Why would you want to name a trust as your IRA beneficiary? It's not a tax-saving move and indeed could increase your tax bill. Still, there are valid reasons for using this planning technique. The primary benefit is protection against the IRA assets being squandered or attached by creditors. For example, you might want to pass money in an IRA to someone who is under age 21 and may not have much experience handling financial affairs or to a family member who is known to be a spendthrift. Having the account pass into a trust could enable a trustee to control how the money is distributed.

In a similar vein, you might intend to provide IRA funds to your spouse in a second or third marriage, but without shortchanging your children from an earlier marriage. In that case, you might leave the assets to a trust that pays out income to support a surviving spouse for life, with the remainder going to the children.

In any of these cases, naming a trust as your IRA beneficiary could be helpful—though, again, you'll need to work with an attorney with specialized knowledge of trusts and estate planning. Having the proper language in documents for the IRA and the trust is crucial.

One key aspect of such an arrangement is that the trust you name as IRA beneficiary should have people—and not an institution or your estate—as its beneficiaries. That could enable those beneficiaries to use "stretch IRA" planning techniques to lengthen the amount of time that assets can utilize an IRA's tax advantages. Although required minimum distributions (RMDs) still will have to happen, they'll be based on the life expectancies of the ultimate beneficiaries. The younger they are, the longer the money can be shielded from taxes. If more than one nonspouse beneficiary is named in a trust, the age of the oldest living beneficiary must be used. Consider separate trusts for each nonspouse beneficiary.

A variation on this theme calls for naming your spouse as the primary beneficiary and the trust as the contingent beneficiary. Such a setup provides greater flexibility because the surviving spouse may roll over the inherited IRA assets into his or her own IRA as part of post-mortem estate planning. ●

Avoid These 6 Mistakes

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strategy may be preferable if you don't need the money and you intend to pass along the inherited assets to younger beneficiaries eventually. Doing it now means RMDs will be based on the new owner's longer life expectancy.

Mistake #4: You fail to analyze contingent beneficiaries when using a disclaimer. It's important to consider all relevant financial and tax factors before agreeing to pass up inherited IRA assets through a disclaimer. This is not a casual decision. Consider whether the contingent beneficiaries in fact will be able to stretch out the IRA longer under their life expectancies and look at their tax consequences. Younger contingent beneficiaries may be in a lower tax bracket than you are, and if they pay the taxes that could reduce the overall tax bite.

Mistake #5: You take a lump-sum distribution. Some people think they're required to take a lump-sum distribution from an inherited IRA to empty the account immediately. That's simply not true. If you need the money, go ahead and take it. But if you don't have a pressing need, going the stretch IRA route could enable you to preserve wealth longer and generally will reduce tax liability.

A large lump-sum distribution could rocket you into a higher tax bracket and force you to lose more of the inheritance in taxes.

Mistake #6: You fail to analyze spousal rollovers. Current tax law offers greater flexibility to spouses who inherit an IRA. They can roll over inherited assets into their own IRA accounts and set up payouts calculated on their own life expectancies. However, a rollover isn't always the optimal approach for spouses. For instance, if a surviving spouse is under age 59½, payouts from the IRA will trigger the 10% penalty tax for early withdrawals, on top of the regular income tax owed. ●

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