



Chicago Estate Planning Council

To ensure your CE Credit, be sure to return this form following meeting.

INSURANCE

CONTINUING EDUCATION CERTIFICATE OF COMPLETION

Name of Attendee or Completer _____

Social Security Number _____

Company _____

Business Telephone # _____

Address _____

Name of Program **"WHY I HATE IRA'S AND WHY YOU SHOULD TOO"**

Name of Sponsor Chicago Estate Planning Council

Location of Program The Standard Club

Date of Completion SEPTEMBER 18, 2008

Number of contacts hours One (1) Credit Hour

I certify that the individual above attended/completed the CE Program/Course on the date(s) as indicated.

SEPTEMBER 18, 2008

Date

Authorized Signature of On-Site Coordinator

Return to:

CEPC

401 N. Michigan Avenue-22nd Floor

Chicago, IL 60611-4267

Tel: 312-673-4707; Fax: 312-673-6964

E-Mail: cepc@smithbucklin.com

ATTORNEY—FORM A

For validation of CPE hours, this form must be returned to the Chicago Estate Planning Council following this session.

Name of Attendee or Completer _____

Company _____ Tel #: _____

Address _____

Name of Program: "WHY I HATE IRA'S AND WHY YOU SHOULD TOO"

Name of Sponsor Chicago Estate Planning Council

Location of Program The Standard Club

Date of Completion SEPTEMBER 18, 2008

Number of Contact Hours One (1) Hour

I certify that the individual identified above attended/completed the CE program/course on the date(s) as indicated.

SEPTEMBER 18, 2008
Date


Authorized Signature of On-Site Coordinator

ATTORNEY—FORM B

PARTICIPANT'S RECORD OF ATTENDANCE

(KEEP WITH YOUR MCLE RECORDS)

Name of Attendee or Completer _____

Company _____ Tel #: _____

Address _____

Name of Program: "WHY I HATE IRA'S AND WHY YOU SHOULD TOO"

Name of Sponsor Chicago Estate Planning Council

Location of Program The Standard Club

Date of Completion SEPTEMBER 18, 2008

Number of Contact Hours One (1) Hour

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SEPTEMBER 18, 2008
Date


Authorized Signature of On-Site Coordinator



Chicago Estate Planning Council
401 N. Michigan Ave, Chicago, IL 60611
Tel: 312-673-4707; Fax: 312-673-6964

CPA -- FORM A

Program Evaluation and CEPC Verification of Attendance

For validation of CPE hours, this form must be returned to the Chicago Estate Planning Council following this session.

(Return to the CEPC Support Staff)

Program: Chicago Estate Planning Council

Session Title: **"WHY I HATE IRA'S AND WHY YOU SHOULD TOO"**

Date: SEPTEMBER 18, 2008 Time: Noon CPE Hours: One (1) Credit Hour

PLEASE PRINT NEATLY

Name _____

Company Name _____

Street Address _____

City/State/Zip _____ Phone _____



Chicago Estate Planning Council
401 N. Michigan Ave., Chicago, IL 60611
Tel: 312-673-4707; Fax: 312-673-6964

CPA -- FORM B

Participant's Record of Attendance

(Keep with your CPE Records)

Program Chicago Estate Planning Council

Session Title "WHY I HATE IRA'S AND WHY YOU SHOULD TOO"

Date: SEPTEMBER 18, 2008 CPE Hours One (1) Credit Hour

Name _____

Company _____

Address _____

Information for program participants on the retention of CPE records:
Participants are advised that the widely adopted 1976 Statement on (CPE) Standards places responsibility on both the individual participant and the program sponsor to maintain a record of attendance at a program.
The information the participant should keep on each program is: a) sponsor's name, b) title and/or description of content, c) date(s) of the program; d) location; and e) number of CPE contact hours.
The record should be kept for an appropriate period to allow regular periodic reporting to jurisdictional board(s) to accountancy and to professional organizations requiring such reports. Sponsors are required to keep documentation on programs for five years.
Some State boards request copies of this information directly from registrants, others will confirm with the program sponsor those details provided by participants on a registration form.
Retain Form B for your records. Verification of CPE hours is complete only if Form A is returned to the Chicago Estate Planning Council.

Michelle Mallick
Signature

EXEC. DIRECTOR SEPTEMBER 18, 2008
Title Date

SPONSOR FORM

TO: BOARD OF DIRECTORS
CHICAGO ESTATE PLANNING COUNCIL

Date: _____

RE: MEMBERSHIP APPLICATION FOR:

Name	Telephone #
Firm/Organization	

I am personally acquainted with the above applicant and believe this applicant has sound professional ethics. As a member of the Chicago Estate Planning Council I feel this applicant will be a credit to the Council and will make a responsible contribution to the Council.

Additional Information:

1. Length of time acquainted with applicant: _____
2. Is applicant a member of your firm? _____
3. Describe your contact with the applicant in estate planning matters: (use separate sheet for additional information)

Article I of the CEPC By-Laws states as follows:

The purposes for which the Council is organized are:

- 1) *To maintain the highest standards of service in providing informed guidance in the creation, conservation, and distribution of estates;*
- 2) *To continue and further the education of its members and the public in estate planning matters;*
- 3) *To increase public understanding of the need for competent estate planning;*
- 4) *To promote cooperation, and to foster a better understanding of the proper relationship among estate planning specialists from different fields and to bring together in one association those specialists who have a common interest in promoting the Council's purposes;*
- 5) *To encourage the highest standards of ethical conduct.*

By signing this sponsorship form, you acknowledge that you believe the applicant possesses the professional expertise and the ethical standards consistent with the purposes of the Council as set forth in the By-Laws.

I recommend approval of the above applicant. I am pleased to sponsor the membership, and I believe the applicant will further the purposes of the Council.

Signature of Sponsor	_____ Attorney, ChFC, CFP, CLU, CPA, TR
	Designation (circle one above)

Sponsor's Name (Please Print)	_____ Telephone Number
-------------------------------	---------------------------

Sponsor's Firm

Chicago Estate Planning Council, 401 N. Michigan Avenue, 22nd Floor, Chicago, Illinois 60611-4267
Telephone: 312-673-4707; Fax: 312-673-6964; E-Mail: cepec@sba.com

CHICAGO ESTATE PLANNING COUNCIL

**THURSDAY, SEPTEMBER 18, 2008 – LUNCH AT NOON
THE STANDARD CLUB, 320 S. PLYMOUTH COURT, 5TH FLOOR, CHICAGO, IL**

**“WHY I HATE IRA’S AND WHY YOU SHOULD TOO”
ELLIOTT M. FRIEDMAN, FRIEDMAN & HUEY ASSOCIATES LLP**

Check One: _____ Members _____ Guest

Circle Your Discipline: Attorney ChFC CLU CFP CPA TR Other _____

EVALUATION

Please *circle* the number which most accurately reflects your evaluation and provide comments, as appropriate.
(5 = Excellent; 3 = Average; and 1 = Poor)

	Rating	Comments
<u>SPEAKER</u>		
Knowledge of Subject Matter	5 4 3 2 1	_____
Presentation Skills	5 4 3 2 1	_____
Relevance of Topic	5 4 3 2 1	_____
Depth of Treatment	5 4 3 2 1	_____
Quality of Handout Materials	5 4 3 2 1	_____
Other Comments		_____
<u>LUNCHEON</u>		
Overall Quality of Food	5 4 3 2 1	_____
Other Comments		_____

CEPC



COMMITTEE(S) VOLUNTEER FORM

Yes, I would be interested in serving on the following committee(s):

Advertising & Sponsorship Committee

Annual Outing Committee

Membership Committee

Reception Committee

Website Committee

Young Members Initiatives Committee

Please print:

Name

Company

Address

City/State/Zip

Telephone

Fax

E-Mail Address

Please return this form to CEPC Registration Desk or mail to:

CEPC
401 N. Michigan Avenue-22nd Floor
Chicago, IL 60611-4267
Attn: Kathleen Callahan
Tel: 312-673-4707
Fax: 312-673-6964
E-Mail: cepc@smithbucklin.com
www.cepcweb.org

CEPC 2008-09 LUNCHEON PROGRAM SCHEDULE

- SEPTEMBER 18 "WHY I HATE IRA'S AND WHY YOU SHOULD TOO"
AUSTIN FLEMING AWARD RECIPIENT
Sponsored by Altair Advisers LLC
- OCTOBER 15 "PREMIUM FINANCING AND LIFE SETTLEMENTS....
THE GOOD, THE BAD AND THE REALLY UGLY"
Howard Sharfman, Schwartz Benefit Services, Inc.
Sponsored by Park National Bank
- NOVEMBER 20 "ASSET PROTECTION STRATEGIES FROM WALL STREET TO MAIN STREET"
Jeffrey Zaluda, Horwood, Marcus & Berk Chartered
Sponsored by Christie's Fine Art Auctioneers
- DECEMBER 17 "PLANNING FOR THE SUPER ELDERLY"
Thomas Abendroth, Schiff Hardin, LLP
Sponsored by Stout Risius Ross, Inc.
- JANUARY 22 "VALUATION: CURRENT COMPLEXITIES, CONUNDRUMS, CONFUSION AND
COURT CASES"
Craig Stout, Stout Risius Ross, Inc.
Sponsored by Life Care Innovations, Inc.
- FEBRUARY 18 "2008 RECENT DEVELOPMENTS
Robert Hamilton, Hamilton Thies Lorch & Hagnell LLP
Sponsored by The Northern Trust Company
- MARCH 18 "HOT TOPICS"
Dennis Belcher, McGuire Woods LLP
Sponsored by JPMorgan
- APRIL 23 "ESTATE PLANNING FOR THE UNMARRIED COUPLE"
Wendy Goffe, Graham & Dunn PC
Sponsored by Harris Bank, N.A.
- MAY 13 "NAVIGATING CONFLICTS IN MULTI-GENERATIONAL PLANNING"
Susan Porter, Bank of America
Sponsored by U.S. Trust, Bank of America Private Wealth Management

WHY I HATE IRA'S AND WHY YOU SHOULD TOO

**For presentation Thursday, September 18, 2008
Chicago Estate Planning Council
Chicago, IL**

**Elliott M. Friedman
Friedman & Huey Associates LLP**

WHY I HATE IRA'S AND WHY YOU SHOULD TOO

Elliott M. Friedman, Friedman & Huey Associates LLP, Homewood & Park Ridge

- I. A tiptoe through the history of IRA's
 - A. The original IRA created in 1974
 1. Designed to accomplish two purposes
 - a. Give workers with no retirement plan a way to save for retirement
 - b. Preserve employer sponsored plan assets by allowing rollover at job change or retirement
 2. Limit was \$1,500 or 15% of compensation
 - B. Revenue Act of 1978 - The SEP-IRA was created to overcome the inertia of small businesses that did not want to wade through the quagmire of setting up qualified plans
 - C. ERTA (Economic Recovery Act of 1981)
 1. Raised limit to lesser of \$2,000 or 100% of compensation
 2. Anyone with earned income can make a contribution
 - D. TRA 1986 (Tax Reform Act of 1986) – Limited who could make deductible contributions to IRA's
 1. Lower income workers could make tax-deductible contributions even if covered by a plan
 2. Permitted non-deductible IRA contributions regardless of whether covered by an employer plan
 3. Both spouses were limited if either was covered by a plan
 4. NOTE: The new rules eliminated simplicity and reduced the use of IRA's even among those who were eligible
 - E. Small Business Jobs Protection Act of 1996 –
 1. Created the SIMPLE (Savings Incentive Match Plan for Employees, for those of you who didn't know what SIMPLE stands for) for small businesses

2. Applies only to businesses with fewer than 100 employees

F. Taxpayer Relief Act of 1997

1. Created the Roth IRA, named for Senator William J. Roth, Jr.
 - a. Contributions not deductible from current income
 - b. Investment earnings are tax-free
 - c. No requirement for distributions beginning at age 70 ½
 - d. Some rollover from IRA's to Roth IRA's (with resulting tax consequences) allowed
2. Raised income limits for deductibility of regular IRA's
3. Spouses could make contributions even if other spouse covered, but subject to limits

G. 2002 - EGTRRA (Economic Growth and Tax Relief Reconciliation Act of 2001)

1. Increased annual contribution (first time in 20 years – apparently no one thought about inflation in those years), and they keep going up
2. Catch-up contributions for individuals age 50 and over
3. Increased limits on eligible contributions to SEP's from 15% to 25% (which eliminated the need for two plans)

H. Pension Protection Act of 2006

1. Made EGTRRA provisions permanent (otherwise would have sunset'd in 2011)
2. Created Roth 401(k)'s
3. Changed rules for rollovers by non-spouse beneficiaries – can now roll to their own IRA's or to another qualified plan in which the beneficiary is a participant
4. Allows (beginning in 2008) for direct rollover to Roth from 401(k)'s and similar plans if requirements are otherwise met

5. Permitted direct contribution to charity from IRA's for 2006 and 2007 only (mentioned here only to comment on the uselessness of this provision in almost all cases)

I. I can't find the law, but I know it happened – Elimination of the \$100,000 adjusted gross income limitation in 2010 for conversion of traditional IRA's to Roth IRA's

1. Will cause tax of the IRA that would otherwise be taxable income in the year of the rollover
2. Suggests that taxpayers should be building up their IRA's now to take advantage (if that is their plan) in 2010
3. Applies to portions of the IRA that were funded with non-deductible contributions
4. Will allow circumvention of AGI limits for Roth IRA's – make a contribution to a regular IRA and then roll it to a Roth – another well planned Congressional exercise in IRA legislation
5. If your IRA is mostly non-taxable (i.e., funded with non-deductible contributions and the stock market hasn't been good to you), this seems like a no-brainer.

II. The client and the IRA contribution – a 7-part mini-opera of screw-ups

- A. The January 2nd contribution – “I read in the newspaper...”
- B. The Roth contribution – “I read in the paper and estimated my income for the year, and I didn't know I was going to get a K-1, and...”
- C. The “I didn't think I was too old to make an IRA contribution even though I'm over 70 ½” contribution
- D. The in-kind contribution – “I didn't want to sell this stock because it's really going up, and it even went up on the day I transferred it to my IRA”
- E. The January 1st - April 14th of the following year contribution – “I thought you told me...”
- F. The April 14th of the following year contribution – “I read in the newspaper...”

G. The April 15th of the following year contribution – it's 11:59 p.m. – do you know where your IRA contribution is?

1. PLR 8551065 says that an IRA contribution is timely if it is mailed on or before the due date of the return, even if recorded afterward by the financial institution
2. Hopefully the post office will guarantee the postmark of all the mail turned in at the post office on April 15th as opposed to just the mail addressed to a tax authority

III. The deceased client and the IRA

A. The post-death IRA contribution – I can't find anything that says that you can't do this from an income tax standpoint

1. Perhaps reality trumps law – does the executor have the right/power to make such an IRA contribution?
2. Probably a bad idea anyway

B. The post-death IRA required minimum distribution (discussed later, but mentioned now)

IV. Over-contributions to IRA's

A. The maximum contribution amount is the lesser of the "deductible amount" or 100% of compensation (the term deductible amount generically refers to the ceiling on contributions assuming the compensation requirement is met).

B. The deductible amount is provided in a table under IRC Section 219(b)(5) A & B. The actual income tax deduction for a Traditional IRA contribution is subject to MAGI limitations if the individual or that individual's spouse is an "active participant" in another type of retirement plan.

C. An individual's total IRA contributions can be made up of any combination of Traditional deductible, Traditional nondeductible, and Roth (subject to AGI limitations) contributions (depending on the facts associated with a particular taxpayer's situation).

- D. Example: In 2007, Tom, a single 35 year old taxpayer and active participant in his company's profit sharing plan, was paid \$53,000 of compensation. Because Tom is an active participant in another qualified plan, the nondeductible portion of his contribution is calculated as follows:

$$\frac{(\text{MAGI} - \text{Applicable amount})}{\$10,000} * \text{Maximum Deductible Amount}$$

Per IRC 219, the term "applicable dollar amount" \$83,000 beginning in 2007 for a joint return, \$52,000 for a single return, and \$-0- for married filing separately.

$$\text{Calculation: } ((\$53,000 - \$52,000) / \$10,000) * \$4,000 = \$1,400$$

- E. As a result, only 90% of his allowable contributions to Traditional IRA's are deductible. As a result, Tom decides to contribute \$3,600 of his \$4,000 maximum contribution to a Traditional IRA, which is fully deductible and the remaining \$400 to a Roth IRA as opposed to making an additional nondeductible contribution in this amount.
- F. Excess contributions are subject to a 6% excise tax annually, not to exceed 6% of the value of the annuity or account.
- G. If the taxpayers discovers the over-contribution PRIOR TO filing their tax return, the 6% penalty or excise tax can be avoided and the taxpayer has the following options available
1. Remove the excess contribution along with any income attributable to that contribution;
 - a. The net income portion of the amount distributed will be subject to the IRA distribution rules and if the taxpayer has not attained age 59 ½ will be subject to the 10% penalty for early withdrawal; the excess contribution amount will be treated as if it never occurred.
 2. Recharacterize the contribution along with any net income attributable to a different type of IRA (i.e. if a taxpayer made an ineligible Roth contribution, this can be recharacterized as a Traditional IRA contribution). The deadline to recharacterize a Roth contribution to a Traditional contribution or vice versa is the extended due date of the individual's return for such tax year.

H. Computing the net income attributable to the excess contribution (Reg. 1.408-4)

1. "Computation period" means the period beginning on the first day of the taxable year in which the excess contribution is made and ending on the date of the distribution from the account.
2. "Net Income" is the FMV of the balance of the account immediately after the distribution increased by the amount of distributions from the account during the "computation period" and reduced (but not below zero) by the sum of: (A) the FMV of the balance of the account as of the first day of the taxable year in which the excess contribution is made and (B) the contributions to the account made during the "computation period".
3. The amount of net income attributable to the excess contributions is an amount which bears the same ratio to the net income earned by the account during the computation period as the excess contribution bears to the sum of the balance of the account as of the first day of the taxable year in which the excess contribution is made and the total contribution made for such taxable year.

I. If the taxpayers discover the over-contribution POST filing their tax return, the 6% penalty or excise tax must be self assessed, but the taxpayers still have the following options available:

1. Remove only the excess contribution (not including the income attributable to the over-contribution).
2. Apply the excess contribution as part of the subsequent year's contribution.

J. In the case of an excess deductible contribution attributable to the "active participant" limitations, the taxpayer may be able to recharacterize the contribution as a nondeductible contribution and still avoid the 6% excise tax penalty.

1. This is accomplished by filing an amended tax return on Form 1040X showing the recharacterization on Form 8606 with the return.
2. Reclassifying a deductible contribution as a nondeductible contribution may generate additional tax liability.

3. Since the IRS presumes that all distributions from a Traditional IRA were made with pre-tax dollars, the taxpayer must keep records to avoid potential double taxation on any nondeductible contributions upon distribution.

V. Over-contributions to Roth IRA's not withdrawn by the due date(s) of the return(s) – one year or several years

- A. The taxpayer must file a Form 5329 for the year the overcontribution was made and pay the 6% excise tax on the excess portion of the contribution. Since the deadline to recharacterize a Roth IRA contribution has passed, the client's only option is to carryforward the excess contribution to the next tax year.
- B. To the extent that the IRA owner did not utilize his maximum allowable Roth IRA contribution in the subsequent year, a Roth contribution will be deemed to have been made by the taxpayer in this amount, thus reducing the amount of the excess Roth contribution carryforward.
- C. The 6% excise tax must be paid on the excess Roth contribution carryforward that remains unabsorbed by the deemed contribution. This process continues on until the excess contribution is fully absorbed in subsequent years.
- D. A client's ignorance to the complexities of the "supposed to be simple" IRA laws would be quite costly under this scenario.

VI. Improper investments for IRA's – see also UBTI discussion below

- A. IRA's cannot be S Corporation shareholders. IRS provided relief for the S Corp (i.e., no loss of S Corp status) when the situation was discovered and the stock was immediately either redeemed or distributed to the IRA beneficiaries – PLR 200817013
- B. Gold is an acceptable investment in an IRA account (PLR 200732026 which deals with a grantor trust that will hold actual gold bullion and will issue shares in itself which will be held by the IRA. The result was a given but apparently someone wanted to make sure that the grantor trust and share elements wouldn't get in the way of the investment being proper)

VII. Improper (and sometimes proper) rollovers

A. Rev. Proc. 2003-16 provides that in deciding whether or not to grant a waiver of the 60-day rollover requirement, IRS will consider

1. Errors committed by financial institution
2. Inability to complete the rollover because of death, disability, hospitalization, incarceration (?), postal error, restrictions imposed by foreign countries
3. Use of the amounts distributed – was the check cashed?
4. Time elapsed since the distribution occurred

B. PLR 200727023

1. Taxpayer was told by financial institution that if he combined the funds from an expiring CD in his own name and the funds from an expiring CD in his IRA, he would get a higher rate.
2. In a tersely worded ruling, the IRS said:
 - a. There is no evidence to suggest that you were unaware that this was not a rollover
 - b. There was no evidence that the taxpayer intended a rollover
 - c. The fact that the funds were commingled was proof that a rollover was not intended
3. Waiver of the 60-day rollover requirement was not given

C. PLR 200720023 dealt with substantially equal payments

1. Taxpayer was receiving a series of substantially equal payments from his IRA
2. Taxpayer transferred some funds from the IRA from which payments were being received to another IRA – actually did this twice (1999 and 2000) – on the advice of his financial advisor in order to diversify investments
3. Taxpayer continued to receive the “correct” payment from the first IRA.

4. Upon audit by IRS in 2004 and assertion that this was a “modification”, taxpayer paid the penalty and transferred the fund from the other IRA’s back into the first IRA in 2005
 5. The transfers in 1999, 2000 and 2005 are all subject to 10% penalty
- D. PLR 200817059 is another indication that IRS will not go beyond this, although I wouldn’t have given the guy relief either
1. Distribution from decedent’s plan was paid to surviving spouse with tax withheld
 2. Surviving spouse claimed he would have rolled it over had he known that there was a tax liability over and above what was withheld
- E. PLR 200717021 – IRA distribution requested before decedent’s death and received after death by the surviving spouse could be rolled over within 60 days even though the decedent was dead
1. Terrific! But the new IRA didn’t have a beneficiary designated by the decedent, so the distribution period would be the decedent’s life expectancy
 2. However, if the spouse is the sole beneficiary of the estate, then he/she could roll it over into a spousal IRA according to several private rulings.

VIII. Early withdrawals from Roth IRA’s

A. Qualified distributions from Roth IRA’s during lifetime

1. Must meet two qualifications
 - a. Made on or after the IRA owner turns 59 ½, or
 - b. To a beneficiary (or owner’s estate) on or after the date of death (withdrawal made on the way to the funeral – I love this wording), or
 - c. Because IRA owner is disabled, or
 - d. For certain qualified “special purchases, and

- e. Meet five year mandatory holding period beginning with the first year in which a contribution was made and ending on the last day of the fifth consecutive year (including the first year)
 - (1) Roth owner passes away in 2008. He/she made Roth contributions in 2006 and 2007. Beneficiary withdraws the Roth in 2008
 - (2) Looks good, right? Wrong. The “and” in the rule above means that even though the owner died, the beneficiary still has to wait until after the fifth year to take the distribution and not have it be taxable income to the extent of earnings.
 - (3) The beneficiary may have had to take required distributions because of the death of the owner during the intervening period if it’s not the surviving spouse
- 2. If not qualified, taxable to extent there are previously undistributed earnings
- 3. Also subject to a 10% penalty on the taxable portion with exceptions for things like death and disability
- 4. The rules makes sense, but you have to keep them straight
 - b. If the Roth IRA owner meets the 5-year test but not the 59 ½ years old test, the taxable portion is subject to income tax and penalty
 - c. If the Roth IRA owner meets the 59 ½ years old test but not the 5-year test, taxable portion is subject to income tax, but not penalty
 - d. The five-year rule for conversions starts with the year of conversion, and works on a conversion-by-conversion basis, i.e., if there was a conversion in 2006, 2007 and 2008, the five-year rule applies for each conversion.

B. Post-death distributions from Roth IRA's

1. Post-death minimum distribution rules apply to Roth IRA's except for "at-least-as-rapidly" rule
2. Entire interest must be distributed
 - a. By the end of the fifth year after the year of death, or
 - b. To a designated beneficiary over a period not greater than the beneficiary's life expectancy, with distributions starting not later than the end of the calendar year following the year of death
 - c. Special rules for spouses
 - (1) Delay distributions to 70 ½
 - (2) Treat as spouse's own Roth IRA, which then would apply the rules above to the spouse during the spouse's life and at the spouse's death

IX. Incorrect beneficiary designation – note that PLR 200742026 stands for the premise that even if you get a state court to declare who the beneficiary is of an IRA, the IRS may not follow, citing the regs that provide that the beneficiary is he/she who is designated "under the plan"

X. Problems with required minimum distributions

A. Which age do you use?

1. Remember that you use the fair market value on December 31st of the prior year. You are focused on the "prior year"
2. Quote from website – "Joe Retiree, who is 80, a widower...would use the Uniform Lifetime Table...indicates a distribution of 18.7 years for an 80 year old." Anyone know why this could be wrong?
3. The regs – "The applicable distribution period...is determined using the ...employee's age as of the employee's birthday in the relevant distribution calendar year." If only we knew what that meant, everything would be fine

4. Publication 590 (readily available to our clients if they care to read it) – “Your life expectancy or distribution period for the current year can be found next to your age as of your birthday in the current year in the appropriate table”. At last, the definitive answer.
- B. Who gets the minimum distribution in the year of death when the decedent wasn't nice enough to take it before he/she died and was nasty enough to live to age 70 ½?
1. Logic would say it should go to his estate. After all, if he had taken it before he died, it would have passed to his heirs
 2. Logic be damned (but contracts be sacred), the distribution goes to the “designated beneficiary”
- C. A middle of the night question (remember the title of the speech!) – If the client dies during the year in which he/she reaches age 70 ½, can the initial required minimum distribution be delayed until up to April 1st of the ensuing year? Presumably yes, but I can't find where it says it can or can't
- D. What do you do when you don't make the required minimum distribution?
1. There is a 50% penalty for excess accumulation, which is the same thing as saying that you didn't take the money out that you were supposed to take out
 2. Self-assessing the penalty
 - a. You are required to file Form 5329 and assess the penalty. A preparer does not have the ability to ignore this filing requirement since the 5329 is part of the 1040, and the signature line on the 1040 affirms that the return includes all items of which you and/or the taxpayer have knowledge
 - b. The instructions to the 5329 no longer require you to pay the tax if you are asking for abatement of the penalty due to reasonable cause. You can self-assess, but not pay as long as you attach the statement requesting the abatement

- (1) This won't do you much good if you are overpaid by an amount that is greater than the penalty being assessed on the 5329
 - (2) There are an infinite number of reasons why the penalty will be abated
- c. Assuming that you have not paid the penalty, you have a 100% chance of getting a balance due notice from the IRS
- (1) This does not mean that your request for abatement has been acted upon. In fact, there is a 99% chance that it hasn't been reviewed at all because no one did anything with it at the Service Center.
 - (2) The notice is being generated by a section of the Service Center computer that has absolutely no idea what is going on anywhere else in the Service Center. It only knows that there is a balance due as keypunched when the return was received
 - (3) The typical response is to answer the notice with a copy of the request for abatement
- d. Assuming that you have not paid the penalty and responded to the notice as discussed above, there is a 95% chance that you will get another notice from the IRS, this time threatening liens and the confiscation of the client's first-born child if the tax hasn't been paid
- (1) This **STILL DOESN'T** mean that your request for abatement has been acted upon. See c. (1) and (2) above
 - (2) At this point, you will probably send a copy of your last letter
- e. Do **NOT** assume that the request has been acted upon until you get either a letter from the IRS specifically responding to your request for abatement or the (what is usually the automatic-once-they've-read-your-abatement-statement) refund is received

XI. Beneficiary designations

A. Can be individuals, or multiple individuals in varying percentages or amounts, or charities (new)

B. Can be trusts (and here we go again)

1. A “designated beneficiary” for purposes of determining the distribution period under the required distribution rules can be a trust that meets specific requirements.

2. The following requirements must be met for the trust to be considered a permissible beneficiary (1.401(a)(9)-4, A-5 b):

a. Trust must be valid under state law;

b. Trust must be irrevocable or become irrevocable upon death;

c. Trust must have identifiable beneficiaries;

d. Trust instrument or list of ALL beneficiaries must be delivered to IRA custodian by October 31 of the year following IRA owner’s death.

3. Identifiable beneficiaries – “ahh, there’ the rub”

a. Must look at all potential beneficiaries as of September 30th of the year following the year of death

b. Must make sure that they are all individuals with ascertainable life expectancies

(1) Leave to “all grandchildren who have reached age 18, or to estate of grandchild who didn’t reach age 18”

(2) If there is one grandchild age 18 at decedent’s death, we’re OK

(3) If there is any grandchild under 18, an estate could become a beneficiary and therefore the beneficiaries are not identifiable

- c. If this doesn't drive you crazy, nothing will
 - d. Can be a "conduit trust" – requiring all distributions from the IRA to be distributed to a named beneficiary
 - e. Can be separate shares – Trust X creates separate shares for A and B, and the IRA beneficiary designation is "50% to the A Trust under the X Trust and 50% to the B Trust under the X Trust" AND the A and B trusts qualify for look-through
 - f. Although the date for determining all of this is September 30th of the year following the year of death, if a beneficiary dies between the date of decedent's death and September 30th of the following year, that beneficiary still counts
4. If not met, IRA is treated as if it does not have a "designated beneficiary" and must distribute over the remaining life expectancy of the deceased IRA owner, if the owner died post age 70 1/2. If owner died before turning 70 1/2, the IRA must fully distribute within the next 5 years.
5. If met, distribution period is determined under the:
- a. GENERAL RULE: Look through the trust. All current and future beneficiaries (including remaindermen and current income beneficiary) of the trust are considered for purposes of determining the distribution period of the IRA, even though the trust and not the trust's beneficiaries has been deemed the beneficiary of the IRA (this is known as the look through rule – look through the trust to the individual beneficiaries). If the trust has multiple permissible beneficiaries, the distribution period is determined by the age of the oldest beneficiary, or the beneficiary with the shortest life expectancy.
 - b. EXCEPTION: If the trust document specifically directs that all distributions from the IRA be paid to a specific beneficiary, then only this identified beneficiary will be considered in determining the "designated beneficiary" for purposes of determining the distribution period.
6. There are a lot of instruments "out there" which were not designed to meet these requirements which we will be arguing somehow meet these requirements.

C. Multiple beneficiary rules

1. The "Separate account rule" is an exception that allows an IRA to be split into separate accounts, one for each permissible beneficiary. The distribution period is then determined by applying the required minimum distribution rules independently to each account.
2. The result is that the distribution period applicable to each account will be based on the life expectancy of the beneficiary to which the account belongs, as opposed to the life expectancy of the oldest beneficiary.
3. Limitation: the separate account can only be applied if an IRA is left outright to individual beneficiaries. The "separate account" exception is not permitted to be used in conjunction with the "look through" rules applicable to qualifying trusts.
4. If any of the beneficiaries of the trust are non-permissible beneficiaries (any beneficiary other than an individual or a qualifying trust), the distribution period will be determined as if there was no "designated beneficiary" (see b above).
5. Removing non-permissible beneficiaries: Since the "designated beneficiary" is not determined until 9/30 in the year following the death of the IRA owner, those beneficiaries whose entitlement has been fulfilled prior to this date will not be considered in determining the "designated beneficiary" (e.g. if one of the beneficiaries is a charity to receive 25% of total trust assets, if charity is paid in full by 9/30 of the year after death, the charity will be ignored for purposes of determining the distribution period).
 - a. Example: The beneficiary of the mother's IRA is her revocable trust. Per the trust document, at death the trust becomes irrevocable and is to be split equally into grantor trusts, one for each child of hers then living. The mother has already started taking distributions prior to her death.
 - b. Is the trust a qualifying beneficiary? Can the IRA be split into separate accounts one for each trust? Are we able to apply the separate account rule? Whose life expectancy determines the required distribution period?

- c. Ultimately, it was determined that the trust was a qualifying trust. The IRA was split into three equal shares one for each trust. Because the "separate account rule" cannot be applied to trusts, the distribution period was determined under the general rule and the age of the oldest beneficiary must be used across the board.

XII. Unrelated Business Taxable Income

- A. Certain investments although not restricted generate income subject to taxation, thus limiting the tax deferral benefits typically associated with IRAs.
- B. This will come up because your client wants to make an investment and "the only place that I have the money to make this investment is in my IRA". When you hear those words, run for the hills
- C. UBTI or "Unrelated Business Taxable Income" is income generated from a trade or business regularly carried on by the IRA that is not substantially related to the exercise by the IRA of its tax-exempt purpose.
 1. Any trade or business regularly carried on by the IRA would be unrelated to its purpose.
 2. An example of an investment that would generate UBTI is a real estate investment partnership whose income is derived from the purchase and sale of real property in the ordinary course of business. The IRA's share of this income from the partnership would be considered UBTI.
- D. IRC 512(b)(4) further states that any unrelated debt-financed investments will also generate income subject to UBTI.
- E. Rental real estate owned within an IRA for investment purposes would not generate UBTI. However, if there is a mortgage, a portion of the income generated by the rental would be UBTI income to an IRA.
- F. Any income generated by securities purchased on margin would also generate UBTI income to an IRA.
- G. IRC 512(b) specifically excludes the following types of income from the UBTI provisions:
 1. Dividends, interest, annuities, royalties
 2. Most rents from real property

3. Gains from the sale of property other than inventory or property held for sale during the regular course of business.

H. IRA's that generate unrelated business taxable income of more than \$1000 must

1. Acquire an Employer Identification Number
2. Make quarterly estimated tax payments
3. File a Form 990-T by the 15th day of the fourth month following the close of the taxable year
4. The tax rates applicable to UBTI are the same as the rates applicable to estates and trusts.