Arkansas Trust and Wealth Management Mega Conference September 2022

IRA Updates and Clarifications on the SECURE Act 1.0 and New Proposed 2022 Rules and Effects on Beneficiary Payouts

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Training Agenda

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- Plan Type Comparison Charts with Updates
- Back-Door Roth Done Right
- Qualified Charitable Distribution Exemption (QCD)
- Rollovers vs. Transfers – You **MUST** know the difference
- New Categories of Beneficiaries
- Beneficiary Payout Options – SECURE Act 1.0
- Beneficiary Payout Options – 2022 Proposed Regs
- 3 Exceptions to spouse not treating it as his/her own.

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Traditional IRA	Roth IRA
• Must have earned income and file a tax return	• Must have earned income and file a tax return
• Maximum contribution is $6000 (2022) under age 50 and $7000 (2022) age 50 and over (less any regular contributions to a Roth for the same year)	• Maximum contribution is $6000 (2022) under age 50 and $7000 (2022) age 50 and over (less any regular contributions to a Traditional for the same year)
• Contributions may be tax deductible or non-deductible	• Contributions are always non-deductible and subject to MAGI limits
• Interest earned is tax-deferred	• Interest earned is tax-free if withdrawn after 5 years of Roth participation and is considered "qualified" – includes age 59.5, death payment to a beneficiary, disability payment or the first-time homebuyer exception.
• **No age limitation beginning for 2020 contributions if owner/spouse has earned income.**	• No age limit for contributions if the owner/spouse has earned income
• **Required distributions must begin for the year the age of 72 beginning for 2021 RMDs**	• No RMDs required at age to owner or spouse beneficiary treating it as own
• Contribution deadline is the tax filing deadline – not including extensions – **April 18, 2023 for 2022 contributions**	• Contribution deadline is the tax filing deadline – not including extensions — **April 18, 2023 for 2022 contributions**

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Back-Door Roths Done Right

- Client's income is too high to make a regular Roth contribution.
- **Client has NO pre-tax contributions in a Traditional, SEP or SIMPLE IRA**.

1. Make a "regular" contribution to a Traditional up to the annual contribution limit for the contribution year
2. Client will file an IRS form 8606 – Nondeductible Contributions with his/her taxes showing the contribution as "nondeductible" to the Traditional.
3. At any time after the contribution is made, that contribution can be "converted" into the Roth IRA. Only earnings will be taxable.

- If client has any **IRAs that contained pre-tax funds**, the amount converted will take on a pro-rata taxability of pre-tax to after-tax funds in the IRA. In other words, they can't just convert the after-tax portion to a Roth.

Qualified Charitable Distribution Exemptions for IRA Owners and Beneficiaries of Inherited IRAs

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Tax Exemption for Required Minimum Distributions to Qualified Charities were made permanent effective December, 2015.

The following procedures and rules apply:
IRA beneficiaries and IRA account owners who are age **70.5 or older** may take their required minimum distribution amounts or more up to $100,000 by December 31st of the exemption year. The eligible IRA accountholder will instruct the financial institution to make the check payable directly to a qualified charity and, by doing so, may take a tax exemption on the IRA distribution line of their tax return for that amount.

The procedure for Issuing the check and IRS reporting is as follows:

1. The financial institution makes the bank or cashier's check payable **directly to the qualified charity**. The check can be given to the accountholder to mail or the bank may mail it directly to the charity
2. The IRA distribution is reported on a 1099-R in the accountholder's name and SSN as a "normal" distribution for the owner (**IRS code 7**) or **"death" distribution for a beneficiary** (**IRS code "4"**) – **NOT a code "F"** - Charitable Gift Annuity.
3. The accountholder shows the distribution amount on line 4a of his/her 1040 form and shows a zero amount in line 4b (Taxable Amount) if all contributed to the charity with the letters "QCD" if the total distribution was directed to a qualified charity. If only part of distribution was directed the a Qualified Charity, the taxable part not contributed would show in box 4b with QCD to the left.

IRS 2021 1040 Tax Form (Client Responsibility)

4a	IRA distributions	4a	100,000	b Taxable amount . . . QCD .	4b	0

3 Questions to Determine Rollover vs. Transfer

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1. **Where is the money coming from and what type of plan?**
   a. Is it coming from a bank, credit union, brokerage house, insurance company? (This answer is just for general information. It does not affect IRS reporting.)
   b. What type of plan/account is it currently in – Traditional or Roth IRA, Inherited Traditional or Roth IRA, SEP or SIMPLE IRA, Qualified Plan – 401k, 403b, profit sharing, government 457 or just a regular "non-retirement" account?

2. **Where is the money going to and what type of plan?**
   a. Is it going to a bank, credit union, brokerage house, insurance company? (This answer is just for general information. It does not affect IRS reporting.)
   b. What type of plan/account is it going to - Traditional or Roth IRA, Inherited Traditional or Roth IRA, SEP or SIMPLE IRA, Qualified Plan – 401k, 403b, profit sharing, government 457 or just a regular "non-retirement" account?

3. **How is it getting there?**
   a. Check made payable to the customer? (Customer has "access" to the funds)
   b. Check made payable to the financial institution fbo the customer? (No access)
   c. Direct Wire to an IRA account at a financial institution? (No access)

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Distributing Plan Type	Contributing Plan Type	Made payable to accountholder	Made payable to financial institution fbo accountholder
Traditional, SEP, SIMPLE IRA	Traditional, SEP, SIMPLE IRA (after 2 yrs)	Premature/Normal Dist Rollover Contribution	* Transfer Out * Transfer In
Roth IRA	Roth IRA	Premature/Normal Dist Rollover Contribution	* Transfer Out * Transfer In
Qualified Plan – 401k, 403b, 457, Profit Sharing	Traditional, SEP, SIMPLE IRA (after 2 yrs)	Premature/Normal Dist Rollover Contribution	Direct Rollover Out (G) (Direct) Rollover In
Traditional, SEP, SIMPLE IRA	Roth IRA	Premature/Normal Dist Conversion Contribution	Premature/Normal Dist Conversion Contribution
Qualified Plan – 401k, 403b, 457, Profit Sharing	Roth IRA	Premature/Normal Dist Rollover Contribution	Direct Rollover Out (G) (Direct) Rollover In
Roth 401k	Roth IRA	Premature/Normal Dist Rollover Contribution	Direct Rollover Out (H) (Direct) Rollover In
Traditional, SEP, SIMPLE IRA (after 2 yrs)	Qualified Plan – 401k, 403b, 457, Profit Sharing	Not allowed	Direct Rollover Out (G) (Direct) Rollover In
*** Direct Transfers to from IRA to IRA NEVER report to the IRS.**			

QP ROLLOVER VS IRA ROLLOVER VS IRA TRANSFER VS ROTH CONVERSION

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QP ROLLOVER	IRA ROLLOVER	IRA TRANSFER	ROTH CONVERSION
Must be distributed from a 401k, 403b, 457, Profit Sharing or ESOP plan	Must be distributed from an IRA – Traditional, Roth, SEP or SIMPLE plan	Must be distributed from an IRA – Traditional, Roth, SEP or SIMPLE plan	Must be distributed from an IRA – Traditional, Roth, SEP or SIMPLE plan
Check is made payable to the participant or to the financial institution fbo the participant	Check is made payable to the IRA client	Check is made payable to the financial institution fbo the client's IRA	Check is made payable to the participant, or to the financial institution fbo the participant. May be also moved between directly between account at the bank
Distribution by QP as "premature or "normal" on the 1099-R if payable to client.	Distribution by QP as "premature or "normal" on the 1099-R if payable to client	Distribution is coded as a "transfer" and no 1099-R is generated	Distribution by QP as "premature or "normal" on the 1099-R regardless of how it moves from the IRA
Contribution is coded as a (direct) rollover in box 2 of the 5498	Contribution is coded as an (IRA) rollover in box 2 of the 5498	Contribution is not reported and just adds into the IRA account balance	Contribution is coded as a "conversion" contribution and reports in box 3 of the 5498
If check is payable to client, 60 day rule applies	If check is payable to client, 60 day rule applies	No 60 day rule applies	If check is payable to client, 60 day rule applies
Unlimited QP to IRA rollovers in a 12 month period	Only one rollover from IRA to IRA is allowed in a 12 month period	Unlimited IRA to IRA transfers in a 12 month period	Unlimited IRA to Roth IRA conversions in a 12 month period

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New Categories of Beneficiaries

Eligible Designated Beneficiary (EDB)
- Spouse Beneficiary
- Disabled Beneficiary
- Chronically Ill Individual
- Beneficiary of owner who is less than 10 years younger
- Minor child of the IRA owner until he/she reaches age 21

(Non-Eligible) Designated Beneficiary (DB)
- All other nonspouse individual beneficiaries
- Qualified Trust Beneficiary
- Minor child of the owner once he/she reaches age 21

Non-Designated Beneficiaries (NDB)
- Estate
- Revocable Trusts
- Entities

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Beneficiary Payout Options - 2022 Proposed Regulations

Payout Options	**Eligible Designated Beneficiary - Spouse**	**(Non-eligible) Designated Beneficiary and Eligible Designated Beneficiary (Nonspouse)**	**Non-Designated Beneficiary Estate, Revocable Trust or Entity**
1. Lump Sum Distribution (Usually taken at one time)	Yes, available by 12/31 of any year after the owner's death not to exceed 10 years	Yes, available by 12/31 of any year after the owner's death not to exceed 10 years	Yes, available by 12/31 of any year after the owner's death not to exceed 5 years if owner was not in RMD
2. Ten-Year Payout with optional distributions the first 9 years then closed by 12/31 of the 10th year after the owner's death	Yes, available within 10 year period after owner's death if owner had not reached his/her required beginning date. (By April 1st of 73rd year)	Yes, available for both EDB and Non-EDB within 10 year period after owner's death if owner had not reached his/her required beginning date. Distributions are optional in years 1-9 and closed by 12/31 of the 10th year after owner's death for non-eligible beneficiary.. Not available to qualified trust	No. Optional RMDs within first 4 years then closed by end of 5th year after owner's death. Longest allowed if the owner not reached his/her required beginning date and had no designated beneficiary on the IRA.
3. Payout over Single Life Expectancy From Inherited IRA (Default designated EDB beneficiary payout. Usually over beneficiary age if owner was not in RMD, or over the younger of owner or beneficiary age if owner was in RMD.	Yes, if treating it as Inherited IRA and deceased spouse was younger than the surviving spouse and not in RMD. The year the deceased spouse would have attained the age of 72, use the spouse benef's age each year on the SLE. NEW! Spouse can only treat it as his/her own no later than the year when the deceased spouse would have turned 72.	**If the owner was not in RMD** at time of death and EDB is not choosing the 10-year payout, the nonspouse EDB must begin SLE payout the year after the owner died and take a distribution each year with divisor reduced by one. Successor beneficiary continues SLE and accelerates to close 10 years after the original EDB beneficiary dies. **If the owner was in RMD** at the time of death, the EDB and the designated beneficiary must begin SLE payout the year after the owner died based on the longer of the owner or beneficiary's SLE reduced by one each year. The non-EDB must have the IRA closed by 12/31 of the 10th year after the owner died. The successor beneficiary of an EDB must have the IRA closed by 12/31 of the 10th year after the EDB died.	Yes, but only if the owner was in RMD when deceased. The payout must be calculated on the deceased owner's remaining single life expectancy the year the owner died, reduced by one each year and divided into the prior year-end balance. Must begin no later than the year after the owner died. Can always take it out faster.
4. Transfer into Beneficiary's Own Name (Only available to spouse beneficiary)	Yes, available if the spouse is the beneficiary of the IRA and the surviving spouse had not started mandatory SLE payments from an Inherited IRA.	No, never available into nonspouse beneficiary's own name, only into an "Inherited IRA" styling "John Doe, beneficiary of Mom Doe" "Doe Trust, beneficiary of Mom Doe"	No, never available into nonspouse beneficiary's own name, only into an "Inherited IRA" styling "Estate of John Doe, beneficiary of John Doe's IRA

Qualified Trust Definition

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1. Trust is valid under state law,
2. Trust is irrevocable or becomes irrevocable at the owner's death,
3. Beneficiaries are all individuals by Sept 30th of the year after death, and clearly indicated in the trust document, and
4. The bank is provided as copy of the trust document by 10/31 of the year after the owner's death.

Multi-Beneficiary Trusts

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Applicable multi-beneficiary trusts —

- (1) *General definition of an applicable multi-beneficiary trust*. An applicable multi-beneficiary trust is a see-through trust with more than one beneficiary and with respect to which—
- (i) All of the trust beneficiaries are designated beneficiaries; and
- (ii) At least one of the trust beneficiaries is an eligible designated beneficiary who is disabled (as defined in paragraph (e)(1)(iii) of this section) or chronically ill (as defined in paragraph (e)(1)(iv) of this section).

Multi-Beneficiary Trust - Type I

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Qualified See-Through Multi-Beneficiary Trust – Type I

- Trust is valid under state law, is irrevocable or becomes irrevocable at the owner's death, beneficiaries are clearly indicated in the trust document and the bank is provided as copy of the trust document by 10/31 of the year after the owner's death.
- Trust Splits into separate sub-trust for each beneficiary when owner dies with separate EINs
- Each sub-trust beneficiary is treated as if he/she were the IRA owner's designated beneficiary for payout options:
  - Eligible Designated Beneficiary - takes single life expectancy payout beginning the year after the owner dies and then accelerated to 10-years after EDB's Death
  - Non-Eligible Designated Beneficiary – takes single life expectancy over the oldest trust beneficiary's single life reduced by one and closed by 12/31 of the 10th year after the owner dies.

Multi-Beneficiary - Type II

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Qualified See-Through Multi-Beneficiary Trust – Type II

- If all beneficiaries of trust are individuals and are Eligible Designated Beneficiary due to disability or chronically ill and no other beneficiaries have any rights to the IRA until the EDB dies, distributions can be calculated on the oldest EDB's single life expectancy reduced by one and must be completely paid out by 12/31 of the 10th year after the last Eligible Designated Beneficiary of the Type II trust dies.
- If any of the beneficiaries above is a minor child of the owner, the trust can take single life payments until 10 years after the minor reaches age 21 at which time the IRA must be completely paid out.
- If all the beneficiaries are (non-eligible) designated beneficiaries, the trust can calculate single life expectancy payouts reduced by one each year based on the oldest trust beneficiary's age in years 1-9 and accelerated to close10-years after oldest trust beneficiary dies.

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Spousal Options: Treat as Own or Treat an Inherited IRA

- Many financial institutions automatically put decedent spouse's IRA into an Inherited IRA for the surviving spouse instead of treating it as his/her own.
- This can cause extra taxes being paid because inherited IRAs use the Single Life Expectancy Table I and the owner's own IRA uses the Uniform Lifetime Table III – which has a built-in joint life expectancy of 10 years between the owner and a younger beneficiary – resulting in a longer payout and less taxes paid each year.
- Also results in the successor beneficiary of the Inherited IRAs taking expedited payouts using the original beneficiary's (or in some cases the deceased owner's) remaining Single Life Expectancy.
- Because of this, 99% of the time a spouse should just treat it as his/her own.
- If they have an existing IRA in their own name, transfer out of the decedent and transfer into the spouse IRA. No reporting is generated
- If no IRA in their own name, open them a new plan using regular IRA documents (as opposed to Inherited IRA documents) titling it in just the surviving spouse's name – not "beneficiary of deceased spouse" and do the transfer.
- On the next two slides, there are 3 exceptions to a spouse beneficiary not treating it as his/her own: 1) FDIC 2) Surviving spouse is under age 59.5 3) Surviving spouse is older than deceased spouse who was not in RMD at death

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3 Exceptions to Spouse Beneficiary Treating the IRA as his/her own

1.

Husband Dies First

Husband – Age 62
$200,000 balance

Wife – Age 52
$200,000 Balance

OR

$400,000 – Over FDIC Limit

Wife Beneficiary of Husband – Separately Insured

2.

Husband Dies First

Husband – Age 62
$100,000 balance

Wife – Age 52
$100,000 Balance

OR

Wife needs money in next 8 years – Premature Distribution
Taxable **plus 10% Penalty**

Wife Beneficiary of Husband – Death Distributions – Penalty Free
When spouse attains the age of 59.5, no reason to keep as Inherited.
Transfer into her own name at 59.5

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3 Exceptions to Spouse Beneficiary Treating the IRA as his/her own

<u>Husband Dies First</u>

3. Husband – Age 62
$100,000 balance

Wife – Age 73
$100,000 Balance

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Wife Beneficiary of Husband – Wife can postpone distributions for 10 years until deceased spouse would be age 72.
If stays as Inherited IRA after that time, RMDs are based on the Single Life Expectancy. Or, transfer to spouse's own IRA when deceased spouse would have been 72 and Uniform Lifetime Table III can be used resulting in longer payout

Wife has to take RMDs on both balances added together.

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Thank You for Attending

Follow-up questions may be directed to:

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