Steve Leimberg's Estate Planning Email Newsletter - Archive Message #3099

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From: Steve Leimberg's Estate Planning Newsletter

Subject: **Mary E. Vandenack, Joy Matak & Martin M. Shenkman: Notes from the 58th Heckerling Institute on Estate Planning - Part 4**

The **58th Heckerling Institute on Estate Planning** was held January 8 through January 12, at Marriott World Center in Orlando, Florida. Members should click this link to review the meeting agenda: Heckerling. The Heckerling Institute on Estate Planning covers a range of topics for estate planning professionals, including practical pointers that will assist practitioners whether their clients are high net worth individuals or more moderate net worth clients. **Mary E. Vandenack**, **Joy Matak** and **Martin M. Shenkman** attended the Heckerling Institute on Estate Planning and agreed to share their notes. Because of the length of the proceedings and the detailed notes, the notes are being separated into four parts and will be published as a series.

Mary E. Vandenack, J.D., ACTEC, CAP®, COLPM®, Accredited Estate Planner (Distinguished) is a partner in the Omaha office of **DUGGAN BERTSCH, LLC**. Mary is a highly regarded practitioner in the areas of tax, trusts and estates, private wealth planning, asset protection planning, business exit and succession planning, and philanthropic strategies. Mary's practice serves businesses and business owners, executives, real estate developers and investors, health care providers, companies in the financial industry, and tax-exempt organizations. Mary is a member of Entrepreneurs Organization. Mary is a member of the American Bar Association Real Property Trust and Estate Section where she serves on Council. Mary is a member of the American Bar Association Law Practice Division where she currently serves as Chair. Mary has been named to ABA LTRC Distinguished Women of Legal Tech, received the James Keane Award for e-lawyering, and serves on ABA Standing Committee on Information and Technology Systems. Mary is a frequent writer and speaker on tax, benefits, asset protection planning, and estate planning topics as well as on practice management topics including improving the delivery of legal services, technology in the practice of law and process automation. Mary hosts a podcast called Legal Visionaries. https://maryvandenack.com/podcast/

Martin M. Shenkman, CPA, MBA, PFS, AEP, JD is an attorney in private practice in New York who concentrates on estate planning. He is the author of 42 books and more than 1,200 articles. He is a member of the NAEPC Board of Directors (Emeritus), served on the Board of the American Brain Foundation, the American Cancer Society's National Professional Advisor Network, Weill Cornell Medicine Professional Advisory Council, and is active in other charitable organizations.

Joy Matak, JD, LLM is a **Partner** at **Avelino Law.** She has more than 20 years of diversified experience as a wealth transfer strategist with an extensive background in recommending and implementing advantageous tax strategies for multi-generational wealth families, owners of closely-held businesses, and high-net-worth individuals including complex trust and estate planning. Joy provides clients with wealth transfer strategy planning to accomplish estate and business succession goals. She also performs tax compliance including gift tax, estate tax, and income tax returns for trusts and estates as well as consulting services related to generation skipping including transfer tax planning, asset protection, life insurance structuring, and post-mortem planning. Joy presents at numerous events on topics relevant to wealth transfer strategists including engagements for the ABA Real Property, Trust and Estate Law Section; Wealth Management Magazine; the Estate Planning Council of Northern New Jersey; and the Society of Financial Service Professionals. Joy has authored and co-authored articles for the Tax Management Estates, Gifts and Trusts (BNA) Journal; Leimberg Information Services, Inc. (LISI); and Estate Planning Review The CCH Journal, among others, on a variety of topics including wealth transfer strategies, income taxation of trusts and estates, and business succession planning. Joy recently co-authored a book on the new tax reform law.

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NOTES:

Note, items marked "comment" are added by the authors not the speakers.

CORPORATE TRANSPARENCY ACT: TRUSTEES, FAMILY OFFICES, PRIVATE TRUST COMPANIES

Presenters: Nancy G. Henderson is a founding partner of Henderson, Caverly & Pum LLP, San Diego, California. Jocelyn Margoline Borowsky is a partner with Duane Morris LLP in Wilmington, Delaware. Benetta Y. Park is the president of the family office, Johnson Keland Management, Inc., Racine, Wisconsin.

History and Purpose of the Corporate Transparency Act

- The Corporate Transparency Act ("CTA") was enacted as part of an international fight against money laundering. Generally, the United States has been behind in this fight.

- Legal entities in the United States are generally formed by filing documents with the Secretary of state in which the entity is formed. Typically, the filings do not require disclosure about the individuals who financially benefit from or control the entities. Other than filing an SS-4 and federal income tax returns, most entities don't have federal filing requirements. Those entities that are subject to federal regulation will have federal filing requirements.
- Various versions of the CTA had been introduced but the current Act was enacted in 2020.
- FinCen is charged with administering and enforcing the CTA.
- CTA published a Small Business Compliance Guide in September 2023.

CTA Basics

- The principal objective of the CTA is to create a national database of information about the individuals (referred to in the CTA as "Beneficial Owners") who own, directly or indirectly, a substantial interest in (25%+), or hold substantial control over certain types of domestic and foreign legal entities (referred to in the CTA as "Reporting Companies").
- For domestic Reporting Companies created on or after January 1, 2024, and foreign Reporting Companies first registering in the U.S. on or after January 1, 2024, information must be provided about certain persons who were involved in the legal formation or registration of the Reporting Company (referred to in the CTA as "Company Applicants").
- The information provided by the Reporting Companies about their Beneficial Owners and Company Applicants (Beneficial Ownership Information, or "BOI") will be maintained by FinCEN in a secure national database. Access to the information will only be available to certain law enforcement agencies, taxing authorities, and a limited number of other potential users for specified purposes upon request.
- The CTA applies to corporations, LLCs, and other legal entities created by the filing of a document with a Secretary of State or similar office pursuant to the law of the state in which filed. The CTA also applies to foreign legal entities that register to do business in the U.S.
    - General partnerships, sole proprietorships and trusts are usually not created by a filing with the Secretary of State and hence are not directly subject to reporting. However, if a trust or general partnership owns interests in one or more Reporting Companies, they would be Beneficial Owners and have to report.

Exemptions from CTA

- Large Operating Companies. Legal entities that have significant business operations in the United States (referred to in the CTA Final Regulations as "Large Operating II-B-7 Companies") are not subject to the CTA. To qualify as a Large Operating Company, a legal entity must meet all of the following requirements:

- The legal entity must have an operating presence at a physical location in the United States. This cannot be a PO box. The locations must be owned or leased by the legal entity and distinct from the place of any unaffiliated entities. The location may be a personal residence.
  - The legal entity must have more than 20 full-time employees.
  - The legal entity must have at least $5 million of gross receipts or sales, in the aggregate, based on the income tax return for the prior year.
  - **Comment**: A practical issue is that if a company is close to the cut off and just falls below, it would have to report. Thus, some entities that may exceed these thresholds may still opt to report to avoid missing a filing deadline if employment changes, or sidestep the process of defining how many qualifying employees the company has, etc.
- A church, a charity, a nonprofit entity or other organization described in IRC § 501(c) that is exempt from income tax under IRC § 501(a). Such a legal entity will remain a CTA-exempt entity for a period of 180 days following the loss of its tax-exempt status.
  - Note that the filing requirement is 90 days after formation for new entities formed in 2024. In years after 2024, new entities will have 30 days to report. An entity may not have received confirmation of tax exempt status by the time a CTA report would be due, so it might be prudent for a new entity to file.
- A charitable trust or charitable split interest trust described in IRC § 4947(a)(1) or (2).
- A public accounting firm registered with the Public Company Accounting Oversight Board's Registered Firm's list pursuant to the Sarbanes-Oxley Act of 2002.
- A legal entity that exercises governmental authority on behalf of the U.S., an Indian tribe, a state, or a political subdivision of a state if it is established under U.S. law, tribal law, the law of a state or a political subdivision of a state by a compact between 2 or more states.
- An FDIC insured bank, U.S. credit union, or deposit institution holding company.
- A securities exchange or clearing agency and other Securities Act of 1934 entities.
- A registered investment company and registered investment adviser.
- A venture capital fund adviser that is described in Section 203(1) of the Investment Advisors Act of 1940 and has filed Item 10, Schedule A as well as Schedule B of Part 1A of Form ADV with the SEC.
- An insurance company.
- An insurance producer if authorized by a state, and subject to supervision by the state insurance commissioner or similar state office, but only if the producer has an operating presence in a physical location in the United States.
- An entity registered under the Commodity Exchange Act, including a future commission merchant, introducing broker, commodity pool

operator and commodity trading adviser that is registered with the Commodity Futures Trading Commission.

- A retail foreign exchange dealer registered with the Commodities Futures Trading Commission.
- A regulated public utility within the meaning of IRC § 7701(a)(33)(A) providing telecommunications, electrical power, natural gas, water or sewer services.
- A financial market utility designated by the Financial Stability Oversight Council.
- CTA Exempt Subsidiaries
    - A legal entity whose ownership interests are, directly or indirectly, controlled by, or wholly owned by, one or more of the specified exempt entities discussed paragraphs (a) and (b) immediately above is also a CTA-exempt entity under the so-called Subsidiary Exemption. Any ownership interest in a subsidiary, direct or indirect, by either an individual, a non-exempt entity or a CTA-exempt entity described in paragraph below will cause the entity to lose its exempt subsidiary status.
    - There is no CTA exemption for a parent company or a holding company of a CTA-exempt entity.
- CTA Exempt Entities with No Subsidiary Exemption – The following entities are exempt but not considered "specified exempt entities" meaning that subsidiaries of any of these CTA exempt entities do not qualify for the subsidiary exemption discussed above.
    - A legal entity that operates exclusively to provide financial assistance to, or hold governance rights over, the CTA-exempt non-profit entities and trusts that are described in CTA § 5336(a)(11)(B)(xix).
    - Money transmitting businesses and money services businesses registered with FinCEN.
    - Pooled investment vehicles that are operated or advised by any of the following types of CTA-exempt legal entities: FDIC insured banks, U.S. credit unions and deposit institution holding companies; brokers or dealers in securities; registered investment II-B-12 companies and registered investment advisers; insurance companies; and public accounting firms.
    - Inactive legal entities that are not owned directly or indirectly, in whole or part, by any foreign persons. These are also sometimes referred to as "grandfathered" CTA-exempt legal entities. To be "grandfathered," the legal entity must (a) have been in existence on or before January 1, 2020; (b) not be engaged in an active business; (c) hold no assets (including an interest in another legal entity); (d) not had a change of ownership in the prior 12-month period; and (e) not received, directly or through an affiliated entity, more than $1,000 in the prior 12- month period.\
    - **<u>Comment</u>**: The exception for "inactive" is very harshly drawn and will not exclude from CTA filings entities that from most

perspectives are inactive. The mere holding of a $100 bank account would cause the entity to be "active" and have to file.

Beneficial Owners

- The definition of beneficial owner includes any individual who, directly or indirectly, (a) exercises "substantial control" over a Reporting Company (regardless of any actual "ownership" of the legal entity) or (b) owns or controls 25% or more of the "ownership interests" in the Reporting Company.
- **Comment**: The terminology of the CTA is very confusing and will no doubt cause problems for clients. For someone with no ownership interest to have to be characterized as a "Beneficial Owner" is not intuitive.
- Substantial Control:
  - Seniors officers of Reporting Company.
  - Any individual with the authority to appoint or remove any senior officer or a majority of the Board (or similar body) of a Reporting Company has substantial control.
  - Any individual who otherwise directs, determines or has "substantial influence" over "important decisions" is deemed to have substantial control of a Reporting Company.
  - An individual with "any other form of substantial control" over a Reporting Company is also a Beneficial Owner.
  - Substantial control can be exercised directly or indirectly, and it may be exercisable by a trustee of a trust or other similar arrangement.
- 25% Ownership.
  - The definition of ownership is broadly defined an any instrument, contract, arrangement, understanding, relationship, or other mechanism used to establish ownership.
  - **Comment:** Does a percentage lease make a landlord a beneficial owner of a tenant? Might that determination depend on the terms of the percentage rent structure? What about a loan with an equity kicker or participation feature. There are significant issues in the application of the CTA guidance.
  - With respect to a trust that holds an ownership interest in a Reporting Company, multiple individuals could be deemed to own or control the same ownership interest.
    - An individual trustee of a trust (or similar arrangement), or other individual, with the power to dispose of trust assets, will be deemed to control or own the ownership interest in the Reporting Company held in the trust.
    - The reference to "other individual" in this context implies that individuals serving as investment directors, advisors, or committee members, such as trust protectors or persons holding veto powers over certain actions of the trustee, could be deemed to be beneficial owners depending upon the circumstances.

        - A beneficiary of a trust who is the sole permissible recipient of income and principal of the trust, or who can withdraw substantially all of the assets from the trust, will be deemed to own the ownership interest in the Reporting Company held by the trust.
        - The grantor of any trust will be deemed to control or own the ownership interest in the Reporting Company held by the trust if the grantor has the right to revoke the trust or otherwise withdraw assets from the trust.
        - **<u>Comment:</u>** A power to swap or substitute assets may characterize the holder as a Beneficial Owner. The power to loan trust assets may similarly characterize the power holder as a beneficial owner.
- Ownership and control is determined at the time of filing the report.

Who Is a Company Applicant?

- A "Company Applicant" is defined in the CTA Final Regulations as any individual who files the document with an Applicable Agency that creates a domestic Reporting Company or who first registers a foreign Reporting Company with an Applicable Agency. A Company Applicant is further defined as the individual, if any, who directs or controls the filing of such a document. As few as one, and no more than two individuals (the actual filer and the person directing the filer, or the person preparing the documents and the actual filer of the documents) will need to be identified as "Company Applicants."
- **<u>Comment:</u>** Would using a third party filing service enable counsel to the avoid having to file as a Company Applicant? It is not clear whether the lawyer might still be viewed as "directing" the filer. If counsel has a FinCEN ID number, perhaps filing in all cases may suffice. But if the filing service has two people who file as company applicant does that exempt the attorney involved in planning as to how to address the CTA?

What Must Be Reported?

- The following information must be provided:
    - Full legal name of reporting company as well as any tradename.
    - Street address of principal place of business, or the street address of primary location in the U.S. at which the company engages in business.
    - State, territory, possession, or tribal jurisdiction of domestic Reporting Company's registration. **<u>Comment</u>**: A PDF of for example, the Certificate of Formation for the entity would have to be uploaded to the FinCEN portal.
    - Taxpayer identification number ("TIN") or Employer Identification Number ("EIN") for all domestic reporting companies and that of foreign reporting entity with such a number, otherwise Reporting Company's identification number issued by foreign jurisdiction.
- Reporting Company must provide the following for each Beneficial Owners and Company Applicants:

    - Full legal name and Date of Birth.
    - Individual's resident address. Individuals may notify FINCEN that doing so will create a safety risk and each such request will be reviewed.
    - If a Company Applicant works at an entity that regularly forms business, business address may be used.
    - Image of identifying document from which identifying number was obtained and individual's photograph.
    - If an individual is a beneficial owner related to an exempt CTA entity, Reporting Company may simply provide information about the exempt entity.
    - Individuals and entities that are Beneficial Owners or Applicants will be able to obtain a FinCEN identifier.
    - A Reporting Company may also secure its own FinCEN Identifier but only after submitting its initial report to FinCen.

Filing Deadlines

- Reporting companies created or registered in the United States January 1, 2024 or later shall be required to file within 90 days of notice to the reporting company that it has been formed or the date the applicable agency first provides public notice of such creation.
- Note that entities formed January 1, 2025 or later will have 30 days to file.
- Reporting Companies created prior to January 1, 2024, must file initial reports no later than January 1, 2025. **Comment:** that the January 1, 2025 deadline is critical. Practitioners should advise clients about the filing requirements as soon as practical. By spending time now to review trust instruments for trusts that own interests in entities and foundational documents for entities,, practitioners may be able to identify opportunities to make changes that might reduce filing issues (e.g., a trust protector that cannot be located, or who refuses to cooperate by obtaining a FinCEN ID number or providing BO information). For example, if a person holding a loan power would have to file and the trustee is concerned about that person cooperating, perhaps they may be asked to resign before the Reporting Companies in which the trust holds interests are required to file.
- An entity that was exempt but loses its status for exemption from filing shall have 30 days from the date the entity no longer qualifies for any exemption from filing.

Correcting Reporting Errors

- If any information in a BOI Report filed with FinCEN contains information that is incorrect or inaccurate, the Reporting Company must file a corrected BOI Report within 30 calendar days from when it first becomes aware of, or has reason to know of, the mistake or inaccuracy.
- If an individual applies for a FinCEN Identifier and if the information in that application is incorrect or inaccurate, then that individual must file a corrected application within 30 calendar days from when he or she

first becomes aware of, or has reason to know of, the mistake or inaccuracy.

- If a Reporting Company has secured its own FinCEN Identifier, and if the information in its application is incorrect, the Reporting Company must file a corrected application within 30 calendar days from when it first becomes aware of, or has reason to know of, the mistake or inaccuracy.

Keeping BOI Reports and Applications Up to Date

- It is the responsibility of each Reporting Company to keep its BOI Report current with FinCEN. This is not an annual filing requirement but an "as needed" filing II-B-21 requirement, meaning the BOI Report must be updated by the Reporting Company within 30 calendar days of the following events:
    - Change in Information submitted about Reporting Company. **Comment**: For example the ID, like a driver's license expires and a new one with a new expiration date is obtained, a change in name or address.
    - Change in identify of Beneficial Owners. **Comment**: For example, a minor child attains the age of majority.
    - Any change in information previously submitted with regard to Beneficial Owners.
    - If a Reporting Company is using a FinCEN Identifier for a Beneficial Owner, the obligation to keep the information on that Beneficial Owner up to date falls on the Beneficial Owner and not the Reporting Company. **Comment**: This will generally be the way to go to avoid the reporting company having a filing burden it may not be able to keep. However, that may burden the Beneficial Owner with requirements to update their data with FinCEN forever.

Applying the Corporate Transparency Act to Trusts and Trustees

- Trust and The Ownership Test.
    - Final Regulations provide a descriptive list of individuals who would be considered a Beneficial Owner under the ownership test when a trust owns or controls at least 25% of the ownership interests in a Reporting Company: (a) an individual trustee of the trust; (b) an individual with authority to dispose of trust assets; (c) a beneficiary who is the sole permissible recipient of income and principal from the trust; (d) a beneficiary who has the right to demand a distribution of or withdraw substantially all of the assets in the trust; (e) a grantor of the trust who has the right to revoke the trust; and (f) a grantor of the trust who has the right to withdraw the assets of the trust. The foregoing provisions are not intended to be an exhaustive list of situations related to the ownership test with respect to a trust.
    - The ownership test further contemplates an "aggregation rule," namely, that all of an individual's ownership interests in a Reporting Company are to be taken into account to determine if

the individual meets the 25% threshold, including interests that the individual owns or controls directly or indirectly. 31 CFR § 1010.380(d)(2)(iii) ("In determining whether an individual owns or controls at least 25% of the ownership interests of a reporting company, the total ownership interests that an individual owns or controls, directly or indirectly, shall be calculated as a percentage of the total outstanding ownership interests of the reporting company as follows…")

  - There is no attribution of ownership among family members but the rules do contemplate attribution when an individual owns or controls interests through different vehicles.
  - Additionally, the rules may require that a trustee's interest in a Reporting Company be aggregated for purposes of identifying the Beneficial Owner.

Trust as a Beneficial Owner

- 25% threshold must first be met for trust to be a Beneficial Owner (BO) based on ownership. But if trust controls the entity, e.g., 1% GP interests is in trust, then trust is a BO based on substantial control.
- Trustee who owns legal title is a beneficial owner of the reporting entity.
- Disposition is broad enough to cover distributions.
- Directed trust. Investment advisor has powers and would be a BO. What about person who can replace an investment adviser?
- Trust protector. Powers may make a BO, but it depends on which powers are granted. **Comment:** Consider what this means. You cannot assume that a protector is a BO without reviewing the terms of the trust. That suggests that the process of determining which persons in which trusts must file as BO's could be tedious and specific to each trust.
- Beneficiary of income or principal is BO. Beneficiary who can withdraw substantially all the assets.
- Lifetime LPOA, not testamentary POA since that takes place in the future.
- Swap power. This is a power to withdraw trust property so grantor holding it would have to report as BO. What if third party holds swap power? Is that person a BO if not the grantor? Would seem so even though not on the FinCEN bright line list.
- Crummey power. At beginning of funding of trust this might suffice to trigger BO status.
- 5/5 power. That should not seem to get to power to withdraw substantially all of trust property.
- Multiple Beneficiaries. Is the trust drafted so that there are separate shares? If not each beneficiary may not be a BO.
- Directed Trustee holding bare legal title is more akin to an agent but the FinCEN guidance doesn't address so err on the side of caution and report.

- Aggregation rule. No attribution. If you own 10% and trust of which you are sole income and principal beneficairy owns 15% these are aggregated and you must report as BO.
- Silent trust. Incompatible with disclosure rule. If trustee cannot disclose to beneficairy that they are a beneficiary. That information still must be reported and the fact that the trust is "silent" is irrelevant. **Comment**: What about the fiduciary duties of a trustee under such a trust? What happens?

Responsibility for Reporting

- Reporting Company is responsible to report. It is the manager of the LLC for example, who is responsible.
- Trustee has to give its BOI or FinCEN ID number to the Reporting Company, but it is not their responsibility to file the report. **Comment:** But how will the penalties apply? Should everyone that has to file try to follow up to be sure that the filing was made or at least that someone has assumed responsibility to file?

Protection, Use and Disclosure of Beneficial Ownership Information

- Many professionals have expressed concern related to disclosure of highly sensitive information about owners and applicants. Information reported in a BOI Report or FinCEN Identifier application is confidential. Strict confidentiality, security, and access restrictions on the information are imposed. FinCEN has the responsibility to maintain Beneficial Ownership Information in a secure, nonpublic database. **Comment**: This is another reason all BO's should get their own FinCEN ID Numbers. That way, confidential data does not have to be given to the Reporting Company.If direct BO data is to be given then perhaps this is a reason alone to use an outside filing service that keeps BO information for each BO confidential from everyone else involved with the Reporting Company.
- Information can be requested by a federal agency for national security, intelligence or law enforcement purposes. Information can be requested by a state, local or tribal enforcement agency upon authorization by a court of competent jurisdiction in connection with a civil or criminal case. A federal agency acting on behalf of a foreign prosecutor may request information.
- FinCen indicates that further regulations will be issued. **Comment:** Regardless of the attempts to assure practitioners about confidentiality and limited disclosure, the author does not think the uses for which information can be requested have been sufficiently defined in the narrow manner that would match the intended purposed of the CTA – to prevent money laundering.
- Applying the Rules to Modern Trust Structures
  - Modern trusts often bifurcate trustee duties. Note that these Heckerling commentaries include detailed notes on such bifurcation in the coverage of Michael Gordon's presentation on directed trusts.
  - Any trustee, direction advisor, protector, designated representative or other individual acting on behalf of the trust

(whether a fiduciary under state law or not) who meets the 25% threshold and has the power to dispose of trust assets to a beneficiary and the power to terminate a trust likely brings the individual within the definition of an individual with authority over these decisions.

- Presenter pointed out the importance of reviewing the trust agreement to be clear about the specific role of each advisor as well as the governing agreements of any entities holding assets within the trust. **<u>Comment</u>**: Practitioners may want to go further. If a trust was drafted a decade ago, reviewing the trust instrument now may not inform the practitioner of any issues with the proper administration of the trust. Can a retainer agreement be crafted narrowly so that if a problem with the trust occurs, the practitioner is not responsible? That seems a very fine line to draw. If the practitioner drafted the trust and 10 years later reviewed the trust for CTA purposes, will the practitioner be able to escape unscathed if there are material trust administration issues unknown to the practitioner? Also, without obtaining all documentation on trust modifications and actions (decanting, trustee or other person's resigning, exercise of swap powers, etc.) can the practitioner even be sure of the status of the trust? Some practitioners may opt to insist on a full review of the trust documentation and administration since the time that they were last involved if they are to be involved in CTA assistance.
- Other factors that result in sufficient authority include:
  - Voting power;
  - Substantial authority regarding important decisions such as reorganization, major expenditures, loans, compensation of senior officers, amending governing documents and decision-making authority over significant contracts;
  - The right to remove and replace a majority of the board of directors of the Reporting Company;
  - The right to remove senior officers of the Reporting Company;
  - Grantor with right to revoke trust;
  - Beneficiary who is sole permissible recipient of income and principal of the trust and beneficiary owns or controls at least 25% of ownership interests in Reporting Company;
  - A beneficiary who has the right to demand a distribution of or withdraw substantially all of the trust's assets when the trust and beneficiary own or control at least 25%. This likely includes beneficiaries who have a present power of appointment and a beneficiary holding a Crummey power where the trust is not substantially funded (resulting in power applying to substantial portion of trust property).
- Trustee is not considered to actually own the ownership interest. The Trustee would achieve Beneficial Owner status based on

"control" over the ownership interest. If the trustee does not have such control, then it is questionable whether the trustee is a Beneficial Owner at all. The Trustee might also fit within the intermediary exception.

- Beneficiaries
  - A sole current permissible beneficiary of income and principal is a Beneficial Owner if 25% ownership threshold is met. The regs are not clear on whether information must be reported when there are multiple current permissible beneficiaries but this situation likely results in falling within the inheritance exception (mere expectancy).
  - The regs do not address the situation where the beneficiary has only an income interest or only an interest in principal.
  - A beneficiary with a substantial withdrawal power will be a beneficial owner.
- Grantors
  - A grantor with the power to revoke the trust will be a beneficial owner.
  - A grantor who has the right to withdraw assets of the trust is a beneficial owner but it is unclear whether this applies to a grantor with the power to substitute assets.
- Silent Trusts
  - Trustee may have competing obligations.
  - Regs do not address whether a Designated Representative.
- Trusts rotate roles over time and changes may trigger the need to update (change of situs, change of address of trustee or advisor, beneficiary reaching age where beneficiary has power to control or dispose trust assets, minor coming of age, death of beneficiary or grantor who was beneficial owner).

- Applicability of Exemptions
  - Consider a trust that has a single fiduciary, a bank acting as a trustee, and the trust wholly owns an LLC, which in turn, owns a portfolio of marketable securities and other assets. The LLC is member-managed by the sole member, the trust, by its bank-trustee. The trust itself is not a legal entity and cannot hold legal title to the LLC membership interest. Legal title to the LLC's membership interest is wholly owned by the bank-trustee for the trust. This example potentially illustrates a trust structure that complies with the Subsidiary Exemption.
  - Consider instead the same trust with a member managed LLC and bifurcated trustee duties with the settlor acting as an advisor with the right to sell or distribute the entity interest. Even though a non-exempt person has control, the bank-trustee still owns the entity ownership interest and the Subsidiary Exemption still applies.

- If instead, the LLC is manager managed by the settlor who created the trust, the grantor would be a senior officer. Notwithstanding, if the LLC qualifies as a CTA-exempt entity under the Subsidiary Exemption based on its membership interest being wholly owned by the bank trustee, the beneficial owner definition is inapplicable because the LLC is not a Reporting Company. In other words, once the Subsidiary Exemption is satisfied, analysis of beneficial ownership is foreclosed.
- The presenter suggested that it is unlikely that FinCEN intends an interpretation of the Subsidiary Exemption that treats a trust-owned subsidiary as a CTA exempt entity where a non-exempt person controls the ownership interest of the subsidiary. If the trust agreement vests control of investment or distribution decisions in the hands of a direction adviser (who is not a specified CTA-exempt entity) or if the trust agreement gives a non-exempt person the right to remove and replace the trustee, it seems unlikely that the Subsidiary Exemption would be upheld.

The Impact of the CTA on Family Offices and Private Trust Companies

- The definition of family office varies based on who is providing the definition.
- As a generality, a family office is created by a family or families to provide various services such as tax, fiduciary, and compliance needs; investment management, risk management, estate planning, and trust administration; philanthropic advisement, financial education programs for family members; and family governance and wealth transfer planning. The presenter cited Kirby Rosplock, PhD, The Complete Family Office Handbook, (Bloomberg Press 2014) as a resource.
- Family Office Structures
    - Embedded Family Office. This is a family office within a family owned business.
    - Separate Entity. Such entity is funded by service fees paid by family member clients or entities that are being served by the family office entity.
    - Private Trust Company. Certain states allow for the creation of a private family trust company, which can serve as a trustee for trusts and/or as a family office, directly or through a subsidiary.
    - Many family offices are being structured to have the family office take a profits interest in entities holding investments. This structure is based on the results of *Lender Mgmt, LLC v. Comm'r*, T.C. Memo 2017-246 (the "Lender case").
- CTA Implications on Family Office Structures
    - Embedded Family Office. When the family office is embedded in an operating business, the entity to assess for CTA purposes is the operating business. The question is whether the operating

business is a Reporting Company, and if so, who are the Beneficial Owners.
    - Separate LLC/Corporation. The standard CTA analysis applies. The family office is likely a reporting company absent applicability of an exemption. Consider the Large Operating Company as a possible exemption. Those rules are discussed earlier in this summary.
    - Private Trust Company. A regulated private family trust company may fall within the bank exemption. An unregulated private family trust company likely will not. If the bank exemption does not apply, consider other possible exemptions.
    - Lender structure. In this structure, the family office is the management company. Exemptions to consider include the large operating company exemption and the subsidiary exemption (if the entity is a subsidiary of a regulated private family trust company). An additional exemption to consider is that of the pooled investment vehicle.

Ethical Issues on CTA Compliance

- If you are going to advise clients on CTA who is the client? The entity responsible is the reporting company. Are you representing the reporting company or a beneficial owner. If there are multiple beneficial owners, who are you representing? What if the Beneficial Owner does not want to provide information? If there are conflicts of interest, can they be waived? Can you represent both the BO and Reporting Company?
- See Model Rule 1.7.
- An approach -- Get engagement letter from Reporting Entity and get waivers from Beneficial Owners.
- Be careful to limit time duration of representation. **<u>Comment:</u>** Some practitioners are expressly excluding any responsibility for filing amendments under all circumstances to avoid any ambiguity as to their having responsibility for amendments. Given the difficulties of identifying changes requiring an amendment that may be a prudent step.

Take-a-Ways

- Think about CTA compliance before forming entity. Who are Beneficial Owners and how will you get information?
- FinCEN Identification Numbers is key. Require everyone to get them. This way you avoid Reporting Company having to update information. Note that there is no way to terminate or surrender a FinCEN identification number.
- Update governing documents for Reporting Companies regarding transfer of ownership interests. Before you can transfer you must file Beneficial Ownership information or its not a permitted transfer.
- Have processes in place for CTA compliance. Penalties require willful failure so being able to show you had a procedure and that you did your best may help deflect penalties.
- Watch out for Minor becoming adult.

- When in doubt file. There is no penalty for over reporting.
- Applicant who must file. Attorney who directs filing of creation document is a company applicant along with whoever physically files it. You can only have two company applicants. The person who sent it to secretary of state must be one of them.

SLICING AND DICING FIDUCIARY DUTIES TO DIRECTED TRUSTS

Presenter: Michael M. Gordon is a Director at the Wilmington law firm of Gordon, Fournaris & Mammarella, P.A

What Is a Directed Trust?

- A directed trust is a trust that removes one or more powers or discretions traditionally held by the trustee and vests that power or discretion in a person who is either a special trustee or not a trustee at all. The power or discretion can relate to investment decisions, management decisions, distribution decisions and any other decision affecting the administration of the trust. It is important to consider the statutory framework of the state for which the trust is being drafted although it is also important to consider the possibility of a change of situs.
- In a traditional trust structure, the trustee is vested with three trust functions:
    - investment decisions,
    - distribution decisions, and
    - administration (recordkeeping, tax reporting, etc.).
    - A directed trust takes one of these traditional powers and gives it to another trustee.

What Is the Statutory Framework?

- Uniform Trust Code - Section 808(b): “If the terms of a trust confer upon a person other than the trustee of a revocable trust power to direct certain actions of the trustee, the trustee shall act in accordance with an exercise of the power unless the attempted exercise is manifestly contrary to the terms of the trust or the trustee knows the attempted exercise would constitute a serious breach of a fiduciary duty that the person holding the power owes to the beneficiaries of the trust.”
- Third Restatement - Section 75 of the Third Restatement of Trusts states: ...[I]f the terms of a trust reserve to the settlor or confer upon another a power to direct or otherwise control certain conduct of the trustee, the trustee has a duty to act in accordance with the requirements of the trust provision reserving or conferring the power and to comply with any exercise of that power, unless the attempted exercise is contrary to the terms of the trust or power or the trustee knows or has reason to believe that the attempted exercise violates a fiduciary duty that the power holder owes to the beneficiaries.
- Uniform Directed Trust Act - The UDTA has been adopted in 15 states.

    - Section 6 of the UDTA recognizes, that subject to Section 7, (a) the terms of a trust may grant a power of direction to a trust director, and (b) unless the terms of a trust provide otherwise: (1) a trust director may exercise any further power appropriate to the exercise or non-exercise of a power of direction granted to the director; and (2) trust directors with joint powers must act by majority decision.
- The Delaware Model uses the UDTA but has adopted a more detailed version than most states.
- Types of Advisors:
    - Investment Direction Advisor - An Investment Direction Adviser has the ability to direct the trustee with respect to the investment of the trust assets. This is commonly used when a trust is going to hold a concentrated position.
    - Special Holdings Direction Advisor – The use of this type of advisor is typically when there will be a bifurcation of duties with respect to the assets held in trust. This advisor has the ability to direct the trustee as to the special assets while at the same time allowing the trustee to be responsible for the investment and management of the marketable securities held in the trust.
    - Distribution Advisor - A Distribution Adviser who has the ability to direct the trustee when and how the beneficiaries will receive distributions from the trust based on the standards contained in the trust instrument.
    - Trust Protector - The Trust Protector is vested with key powers that will allow the trust instrument to remain flexible as circumstances change over time. Typical duties include the ability to amend the trust for certain purposes, to change the situs and governing law of the trust, the power to remove, appoint and replace advisors, the ability to convert a trust from grantor trust status to non-grantor trust status, and the power to expand the class of beneficiaries.
    - **Comment:** Other special advisors are Charitable Advisors for clients who structure charitable distributions from the trust. This may be designed with a Charitable Advisor (as part of a Distribution Committee) with fiduciary duty or a Charitable Director without fiduciary duty. Some have used Art Advisers, Insurance Trustees, etc.

Liability and Standard of Care

- Directed Trustees and Direction Advisers.
    - UDTA 9(a) - Subject to subsection (b), a directed trustee shall take reasonable action to comply with a trust director's exercise or nonexercise of a power of direction or further power under Section 6(b)(1), and the trustee is not liable for the action. -
    - UDTA 9(b) - A directed trustee must not comply with the trust director's exercise or non-exercise of a power of direction or further power under Section 6(b)(1) to the extent that by complying the Trustee would engage in willful misconduct.

    - UDTA 11(a) - Unless the terms of a trust provide otherwise, a trustee does not have a duty to monitor a trust director; or inform or give advice to a settlor, beneficiary, trustee, or trust director concerning an instance in which the trustee might have acted differently than the director.
- Liability of Direction Advisor
    - UDTA 8(a) - A trust director has the same fiduciary duty and liability in the exercise or nonexercise of the power (A) if the power is held individually, as a sole trustee in a like position and under similar circumstances; or (B) if the power is held jointly with a trustee or another trust director, as a co-trustee in a like position and under similar circumstances; and (2) the terms of the trust may vary the director's duty or liability to the same extent the terms of the trust could vary the duty or liability of a trustee in a like position and under similar circumstances.
    - UDTA 11(b) - Unless the terms of the trust provide otherwise, a trust director does not have a duty to monitor a trustee or another trust director; or inform or give advice to a settlor, beneficiary, trustee, or another trust director concerning an instance in which the director might have acted differently than a trustee or another trust director.
    - Section 5(a)5 - One issue that often arises is whether a powerholder directing a trustee as to a particular function is serving in a fiduciary or nonfiduciary capacity. The UDTA recognizes the need to permit a trust director to serve in a nonfiduciary capacity but only for federal (not state) tax purposes. Section 5(a)(5) of the UDTA permits the terms of a Trust to provide that a power may be held in a non-fiduciary capacity but 10-8 only when the "power must be held in a non-fiduciary capacity to achieve the settlor's tax objective under the United States Internal Revenue Code of 1986.
- Delaware Model
    - Liability of Trustee:
        - When a trustee acts in accordance with the directions of a trust direction adviser, the trustee will only be liable for its "willful misconduct".
    - Liability of Direction Advisor:
        - Absent express language in the governing instrument such adviser is deemed to serve in a fiduciary capacity and will be held to the prudent person standard. However, Delaware law permits a trust agreement to exculpate and indemnify a fiduciary (including an adviser) for all acts other than those committed with willful misconduct.

Estate Planning Uses of Directed Trusts

- The Springing Completed Gift Asset Protection Trust
    - The client will create the trust in a jurisdiction permitting self-settled asset protection trusts.

- The client will create the trust for the benefit of other beneficiaries (i.e., descendants and possibly spouse).
- The client will have no retained discretionary beneficial interest in the trust and instead an independent powerholder, such as a Trust Protector, will have the ability to add to the class of beneficiaries during the client's lifetime which would include the power to add the client as a discretionary beneficiary.
- **<u>Comment:</u>** Some commentators refer to this as a hybrid-Domestic Asset Protection Trust or hybrid-DAPT.
- Under the "Springing" approach the client would never be added as a beneficiary of the trust if life plays out the way the client anticipates. If unforeseen circumstances arise the Trust Protector could exercise the authority conferred upon the Trust Protector pursuant to the terms of the trust to add the client as a discretionary beneficiary.
- Presenter's view is that this structure will avoid the risk of inclusion in the grantor's estate.
- In order for the "Springing" concept to work, the trust not only needs to be created in a jurisdiction allowing for self-settled asset protection trusts but the trust also should be created in a jurisdiction that allows for directed trusts and permits the direction adviser to serve in a non-fiduciary capacity. The power to expand the class of beneficiaries during the client's lifetime should not be held by the trustee as a trustee serves in a fiduciary capacity. Instead, the power should be held by an independent power holder, such as a Trust Protector, serving in a non-fiduciary capacity so as to create the possibility of the power actually being exercised in the future.
- **<u>Comment</u>**: Consider the SPAT or Special Power of Appointment Trust which some have suggested might be less risky then a DAPT or hybrid-DAPT because the grantor never becomes a beneficiary.

- The Incomplete Gift Non-Grantor Trust ("ING")
  - A grantor can establish a trust in a jurisdiction that allows for the creation of self-settled asset protection trusts, retain a beneficial interest in the trust and have the trust treated as a non-grantor trust for income tax purposes. The trust will typically be an incomplete gift for transfer tax purposes.
  - **<u>Comment</u>**: The IRS has ceased issuing PLRs for INGs. California recently joined New York in enacting restrictions on INGs and some have suggested caution. There are other variations of non-grantor trusts that might be considered.
- Avoiding the Reciprocal Trust Doctrine Through Directed Trusts
  - The reciprocal trust doctrine is a judicially created doctrine developed in response to perceived tax-avoidance strategies where two parties, commonly spouses, create trusts for each other which, practically speaking, allows each lifetime enjoyment over their property while avoiding it being in their

gross estate. Under the reciprocal trust doctrine the beneficiary of the trust at issue is deemed to be the transferor of funds into the trust thereby typically negating any tax benefit. For example, if husband and wife were each to create and fund an identical trust for one another the reciprocal trust doctrine could apply so as to treat husband as being both the grantor and beneficiary of the trust he established and wife as being both the grantor and beneficiary of the trust she established.

  - **Comment**: The consequence of a successful reciprocal trust doctrine attack is the "unwinding" of the two trusts so that as the speaker indicated the settlor spouse would be deemed to have created the intended SLAT not for the spouse but for themselves. Reciprocal trust doctrine cases occurred before self-settled trust jurisdictions existed. If the SLATs are created in self-settled trust jurisdictions and comply with the requirements for a self-settled trust (e.g., signing a solvency affidavit, etc.). if the SLAT is uncrossed it may qualify as a DAPT and the assets remain creditor protected and outside of the client's estate.
  - Establishing Differences with Directed Trusts
    - Create different fiduciary and non-fiduciary positions with different duties.
    - Use a springing feature in one of the trusts.
    - **Comment**: There are numerous other strategies such as differences in beneficiaries, different distribution standards, a 5/5 power in one trust but not in the other, different assets, establishing trusts in different jurisdictions, allowing lapse of time between creation of trusts, etc.

Fiduciary vs. Non-Fiduciary Capacity of Direction Advisor

- Default in DE and other states is fiduciary status but you can draft out of that.
- Trustee must serve in fiduciary capacity, but the others can serve in a non-fiduciary capacity.
- Some suggest not to draft out the fiduciary capacity as that leaves beneficiaries at risk. There are concerns with a trustee in a fiduciary capacity following the direction of a person serving in a non-fiduciary capacity under the theory someone must hold the key trust functions/powers held in a fiduciary capacity.
- Trust protector is the only one where some would have serve in a non-fiduciary capacity because trust protector holds non-traditional fiduciary powers. Some powers given to trust protector may not be exercisable in a fiduciary capacity. For example, if you give the trust protector the power to add beneficiaries that cannot be exercised in a fiduciary capacity.
- **Comment**: If a trust protector has the power to remove and replace the trustee who is the fiduciary in a trust perhaps the trust protector holding that power should be required to act in a fiduciary capacity.

Some of the other powers that are given to a designated person, such as to add beneficiaries, must be held in a non-fiduciary capacity and should perhaps be held by a different person to avoid the issue of the same person acting in both a fiduciary capacity and a non-fiduciary capacity. Some of the issue and confusion may be from referring to the person holding various disparate powers as a trust protector. Perhaps a different person with a different title should be used to, for example, add a beneficiary versus be the "trust protector" with remove and replace and other administrative powers.

- Give trust protector power to convert trust from grantor to non-grantor of the trust. This cannot be held in a fiduciary capacity.
- Comment: Consider liability of attorney if name trust protector as non-fiduciary.

FIDUCIARY CASES

Presenter: Dana C. Fitzsimons, Jr. Mr. Fitzsimons is Managing Director and Senior Fiduciary Counsel at Bessemer Trust.

Trust Accountings

- Salce v. Cardello, 348 Conn. 90 (2023).
    - Trust Accounting required.
    - In terrorem clause. Will said any action removes claimant as a beneficiary.
    - Lawyer made errors on death tax return and refused to fix them.
    - Kids also sued each other.
    - Would violate public policy if beneficiary raises fiduciary errors and the erring trustee could hide behind the In Terrorem clause. The In Terrorem is not enforceable where it would interfere with administration of trust. If brought in bad faith it would be disallowed.
- Estate of Sarah Graham Kenan, 2023 NYLJ LEXIS 962 (Surrogate's Court of New York, New York County 2023).
    - No trust accounting required.
    - Court refused to compel a trust accounting for the time period that was subject to a release agreement signed by beneficiary that included disclosure of the same information that would have been included in the trust accounting.
    - The accounting didn't include a Shareholders' agreement, but beneficiary had negotiated it for five years. This was the same information that would have been included in the trust accounting.
    - Court held it was not in best interests of trust.

Trustee Making Gifts

- Stewart v. Martin, 2023 U.S. Dist. LEXIS 39395 (S.D. Ohio 2023).
- The trustee was found to have breached his fiduciary duties in making distributions from a revocable trust during the life of the settlor because the trustee because the terms of the trust required a written direction before distributions were made and that was not done.

- **Comment**: This is yet another revocable trust/power of attorney abuse case. The likely number of such abuses that are never bought to light is huge. It is vital for aging and infirm clients to build in safeguards. Yet another reminder of the benefits of institutional trustees. Practitioners might encourage clients to create revocable trusts with institutional co- or successor trustees and an independent trust protector, and other steps.

Shortened Period of Liability

- Rogers v. Kemp, 2023 Ark. App. 302 (2023).
- Notice must inform beneficiaries of time period to bring a suit.
- The court held that the failure to inform beneficiary of the time allowed for commencing a proceeding against trustee rendered the notice ineffective to run shortened statute of limitations on claims.
- The fiduciary needed to inform the beneficiaries of 1 year statute to bring suit for the UTC time period to run.
- **Comment**: Any action taken based on the terms of a trust or statute must carefully conform to the requirements of each to be effective.

Distributions

- Bosch v. Kirkby, 2023 IL App (3d) 220483-U (2023).
- The trust included a requirement for the trustee to consider other assets of the beneficairy in determining distributions.
- Since the trustee knew the beneficiary had considerable personal funds, the trustee's decision not to make distributions to pay beneficiary's nursing home expenses was not arbitrary or unreasonable.
- **Comment:** These types of phrases are commonly included in trust documents in a wide variety of formats. This case is a reminder that these phrases have consequences.

SECURE ACT IS NOT A TODDLER ANYMORE

Presenter: Natalie B. Choate. Natalie Choate is an estate planning lawyer, writer, and speaker specializing exclusively in the tax and estate planning treatment of IRAs and other qualified retirement plan accounts.

RMD Rules

- Is death before or after the RBD? This matters a LOT.
- Though SECURE seemed to reduce the differences between the RMD rules for "death before the RBD" and "death after the RBD," the Treasury regulations continue and even increase that difference—with a vengeance. For example, the EDB of a participant who died before his RBD can elect to use the 10-year rule instead of the life expectancy payout. SECURE did not require or even suggest that wrinkle. The EDB of a participant who died after his RBD can't elect the 10-year rule (sorry). A designated beneficiary who is subject to the 10-year rule does not have to take any annual RMDs in years 1-9, just a 100% distribution in Year10...unless the participant died on or after the RBD, in which case such beneficiary DOES have to take annual RMDs in years 1-9.

- Step one in determining RMDs to the beneficiary of an inherited retirement account is determining whether the participant died before or after his "Required Beginning Date" (RBD).
- Unfortunately, the RBD is a moving target and is different for different types of retirement accounts. Not only is the "Applicable Age" different for people born in different years, an individual can have different "RBDs" for his various retirement accounts—one for his traditional IRA (strictly age-based), another for his Roth IRA (there is no RBD for Roth IRAs), another for his 401(k) plan (where he is still working past the "Applicable Age" and does not own more than 5% of the employer)! Starting in 2024, it will be possible for one individual to have different RBDs for different accounts in the same retirement plan thanks to SECURE 2.0.
  - In 2023, the RBD for a "traditional" [i.e., non-Roth] IRA is April 1 of the year after the year the IRA owner turns age 73 [or 70½ if the participant was born before 7/1/1949, or 72 if born between 7/1/49 and 12/31/1950]. Scheduled to increase to 75 in 2033. Because the age for starting RMDs is now a moving target, the official RBD is now April 1 of the year after the year the participant reaches the Applicable Age (70½, 72, 73, etc.).
  - For a qualified retirement plan (such as a 401(k) plan) the RBD is the same as for an IRA if the participant owns more than 5% of the employer ("5% owner"). For a non-5%-owner, it is April 1 following the later of the year the employee retires from the employer that sponsors the plan or the year the employee attains age 73 [or 70½ if born before 7/1/1949 or 72 if born between 7/1/49 and 12/31/1950].
  - Roth IRAs have no RMDs during the account owner's life so death is always before the RBD regardless of age. As of 2023, this does not apply to "designated Roth accounts" (DRACs) in a qualified retirement plan, which are subject to the lifetime RMD rules applicable to qualified plans. However, as a result of SECURE 2.0, it will also be true for DRACs starting in 2024, which will create some anomalous results.

Charitable Giving in Trusts

- Traditional retirement benefits are a good asset to leave to charity. Other heirs will have to pay income taxes when they withdraw money from an inherited retirement plan, but a charity, being income tax exempt, collects the full account tax-free.
- The best way to leave a retirement account to charity is to name the charity as beneficiary on your beneficiary designation form. This account goes directly to charity.
- Include language that says: "This gift shall be funded to the maximum extent possible with my IRA or the proceeds thereof."
- Avoid language referring to "income in respect of a decedent. "IRD might be considered a class of income and an instruction to fund a charitable bequest with a class of income will not be respected for

fiduciary income tax deduction purposes unless it has independent income tax effect.

- The IRS's position is that transferring the IRA in fulfillment of a pecuniary bequest is treated as a sale of the IRA (which would generate equivalent income at the trust level) and of course there is no DNI deduction for a distribution to charity and no charitable deduction either since these bequests do not meet the requirements of § 642. This IRS position appears to directly violate the Code's rules for "income in respect of a decedent"; see ¶ 4.6,03 of Life and Death Planning for Retirement Benefits. However, the trustee can shift IRA income to the residuary charitable beneficiary by transferring a $3 million inherited IRA to the charity intact. See FIT Fact # 7 [Appendix A]. Transfer of an IRA to a residuary beneficiary does not trigger realization of income at the trust level. The charity takes over the IRA and cashes it out tax-free because the charity is income tax-exempt.
- SECURE ACT 2.0 – You can have a charity as a remainder beneficiary of a Type 2 AMBT. A Type 2 AMBT is a trust that provides for a beneficiary who is disabled or chronically ill (designated eligible beneficiary).

Separate Accounts

- You need to know prior December 31 account balance.
- You then need to know the factor to use to calculate the RMD.
- All is clear if an IRA is left to one human being as a "designated beneficiary." But what if the retirement account is left to multiple beneficiaries?
    - The IRS has six different rules for determining type of beneficiary (six for dying before RBD and six for dying after RBD).
- To get separate accounts treatment is to divide the account into separate IRAs by the SAD (separate accounts determination date.) The SAD is December 31 after the year in which the account owner died. You have to divide the account equally by the SAD.

Separate Accounts for Retirement Account Through a Trust

- Since 2002, regulations have provided that "...the separate account rules under A-2 of §1.401(a)(9)-8 are not available to beneficiaries of a trust with respect to the trust's interest in the employee's benefit." Reg. § 1.401(a)(9)-4, A-5(c). In other words, "separate accounts" treatment cannot be allowed for multiple subtrusts (or even separate shares distributed outright to different beneficiaries) created under a single trust (called the "funding trust" in this Outline) unless the subtrusts (or shares) were named directly as beneficiaries of the retirement plan. Since SECURE essentially "overruled" this regulation as it would apply to an Applicable Multi-Beneficiary Trust (AMBT), there was some hope that the Treasury would repeal the regulation altogether. The Proposed Regulations did not do so.
- In the case of a trust that qualifies as a designated beneficiary, and that is named as beneficiary, and that "is to be divided immediately upon the death of the employee into separate trusts for each

beneficiary," each subtrust shall be treated as a separate beneficiary if at least one beneficiary of the funding trust is a D/CI individual.

- This section provides that, except as provided for funding trusts where at least one beneficiary is D/CI, "section 401(a)(9) may not be applied separately to the separate interests of each of the beneficiaries of a" See-through Trust.
- Planning tip: Name subtrusts on the beneficiary designation form. The "solution" for this problem is (as before the proposed regulations) for the participant to name, directly as beneficiaries of his retirement account, the separate sub-trusts or beneficiaries intended to wind up owning the benefits. For example, instead of naming as beneficiary "The Mary Doe Revocable Trust," which immediately upon Mary's death is to split up into three subtrusts, name the subtrusts directly ("I name as my beneficiary the separate trusts established for my children and issue under Article 3 of the Mary Doe Revocable Trust, in the proportions indicated in said Article 3 which is hereby incorporated herein by reference"). If the separate shares or subtrusts are named directly as beneficiary on the beneficiary designation form, then they are entitled to separate accounts treatment, provided the accounting requirements (Prop. Reg. § 1.401(a)(9)-8(a)(2)) and deadline requirement (Prop. Reg. § 1.401(a)(9)-8(a)(1)(ii)) are met.

Dealing With Surviving Spouse

- Although the general rule is that a beneficiary who is required to take life-expectancy-based RMDs must commence such RMDs the year after the year of the participant's death, there is a special rule for the surviving spouse. If the participant died before his first "distribution year" (the age for starting RMDs) the spouse is not required to commence distributions until the later of the year after his death or the year in which he would have reached the "Applicable Age". § 401(a)(9)(B)(iv); Prop. Reg. § 1.401(a)(9)-3(d).
- Unlike other EDBs, the surviving spouse's life expectancy is recalculated annually. The effect of this is to extend the life expectancy, since the life expectancy is not reduced by one year each year; life expectancy extends as the individual lives longer (ask your neighborhood actuary how this works). Because the S/S's life expectancy is recalculated annually, the S/S (while living) will not be required to withdraw 100% of the inherited account until she reaches age 120, when the life expectancy finally drops to one year or less. Thus, unlike other EDBs, the S/S cannot outlive her own life expectancy—unless she lives to age 120.
- The surviving spouse's right to roll over retirement benefits payable to her from an inherited plan or IRA was not changed by SECURE. Briefly, as a reminder, the spousal rollover is not a "minimum distribution" rule; it is a totally separate Code section and concept, so it is not subject to various limitations that can arise under the minimum distribution rules.

- Also, there is no requirement that the spousal rollover occur within a certain time after the participant's death. It could occur one, five, or 10 years after his death or even later.
- Suppose the surviving spouse is approaching or past age 72. If the participant-spouse died before his RBD, and the S/S elects the 10-Year Rule [see #4(C) in this PART 3], then the S/S could effectively delay RMDs for about nine years, then in year 9 of the 10-year payout roll over the inherited account to the S/S's own IRA, thus sidestepping several years of RMDs. Prop. Reg. § 1.402(c)-2(j)(3)(iii) blocks this maneuver: A S/S's rollover, if it occurs in any year after the year she turns age 71, must be reduced by a deemed RMD amount—the cumulative total of what would have been RMDs if the account had belonged to her during the delayed rollover period.
- What if surviving spouse does not roll over an inherited IRA?
- Old Rule: RMDs based on life expectancy based on deceased spouse's age and no RMDs required until decedent would have turned 73.
- New Rule: Spouse subject to same requirement to take distributions in year after decedent's death unless spouse rolls over into inherited IRA.

HOPE THIS HELPS YOU HELP OTHERS MAKE A *POSITIVE* DIFFERENCE!

Mary E. Vandenack

Martin M. Shenkman

Joy Matak

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