CHARITABLE PLANNING WITH RETIREMENT ASSETS

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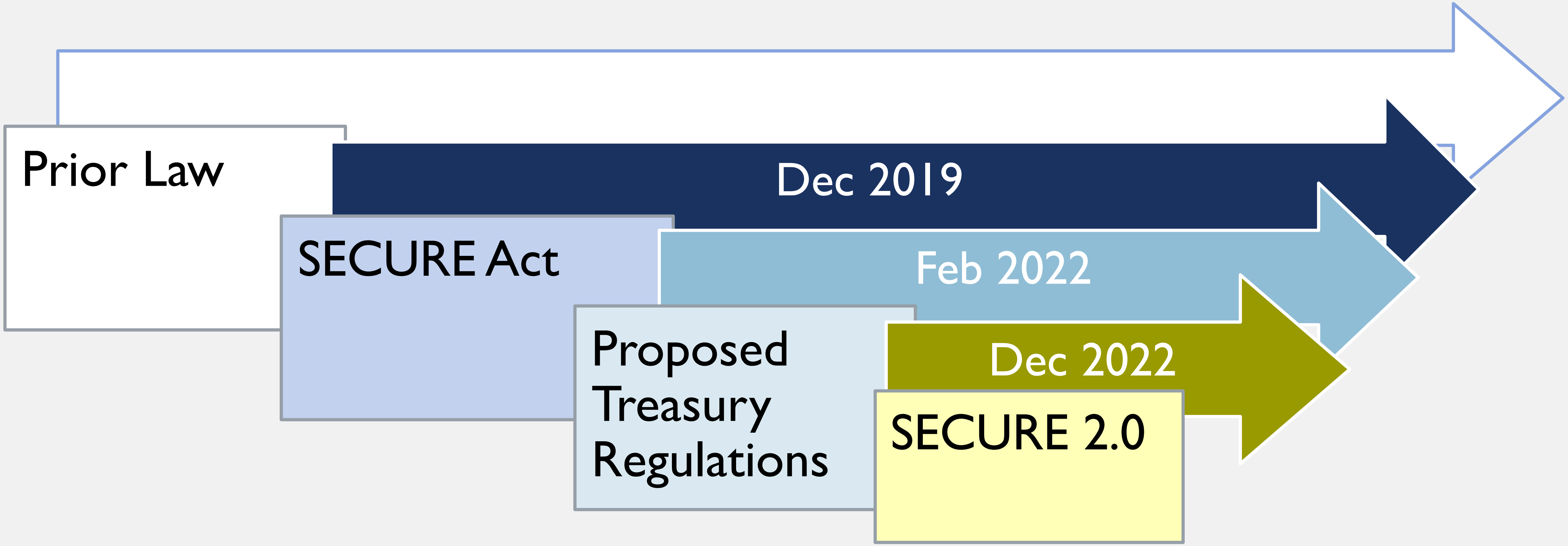
BETTR LAW GROUP

CHANGES TO RETIREMENT PLAN RULES ARE PILING UP



LET'S EXAMINE THE IMPORTANT CHANGES AND DISCUSS CHARITABLE PLANNING OPPORTUNITIES

TRADITIONAL PLANNING WITH RETIREMENT ACCOUNTS

- Since the 1960s, Congress has constructed a system of ***tax-deferred*** retirement plans to facilitate private retirement savings
- To prevent ***indefinite*** deferral of taxable distributions, the Internal Revenue Code & Regulations impose a schedule of ***required minimum distributions*** beginning at the ***required beginning date***
- Distributions from traditional plans are taxable as ***ordinary income***

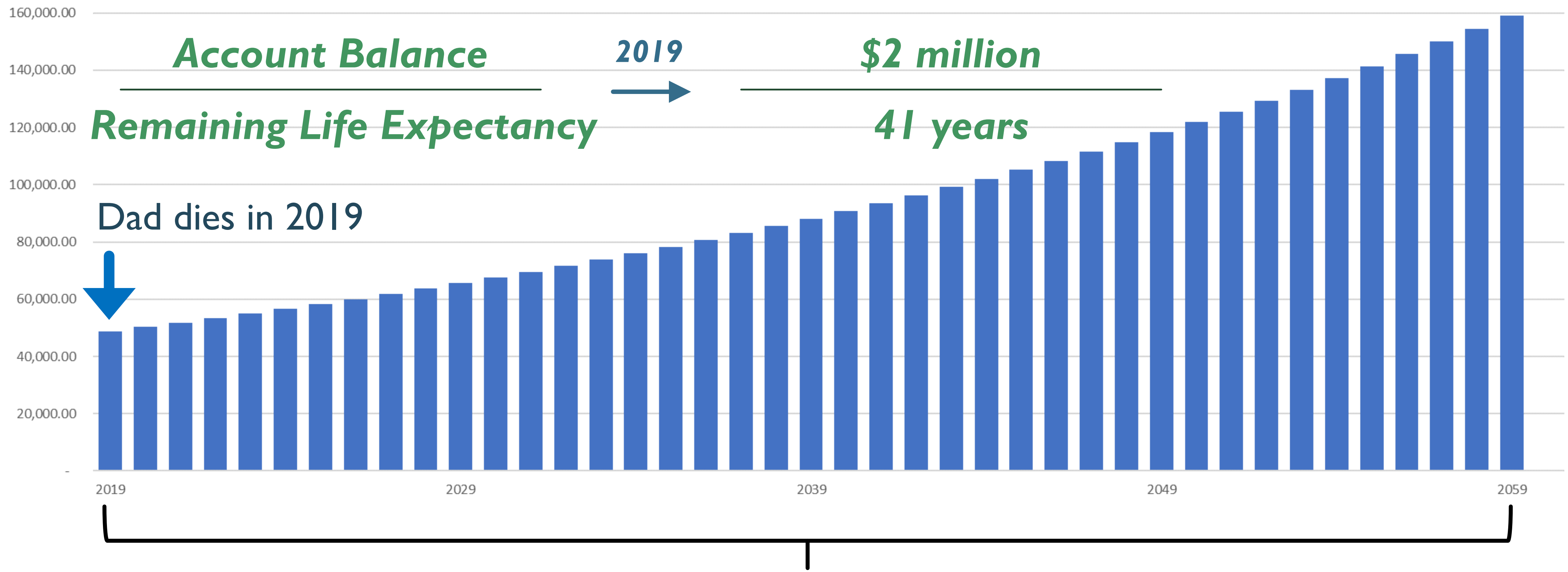
TRADITIONAL PLANNING WITH RETIREMENT ACCOUNTS

"STRETCHING OUT" REQUIRED DISTRIBUTIONS

- Before the SECURE Act, the period for making distributions was generally based on the life expectancy of the designated beneficiary or the participant
  - If no individual was designated, a 5-year distribution period applied in certain cases
- Families that successfully "stretch out" distributions over the beneficiaries' lifetimes may achieve ***significant tax savings***.

Blue = Required Distribution

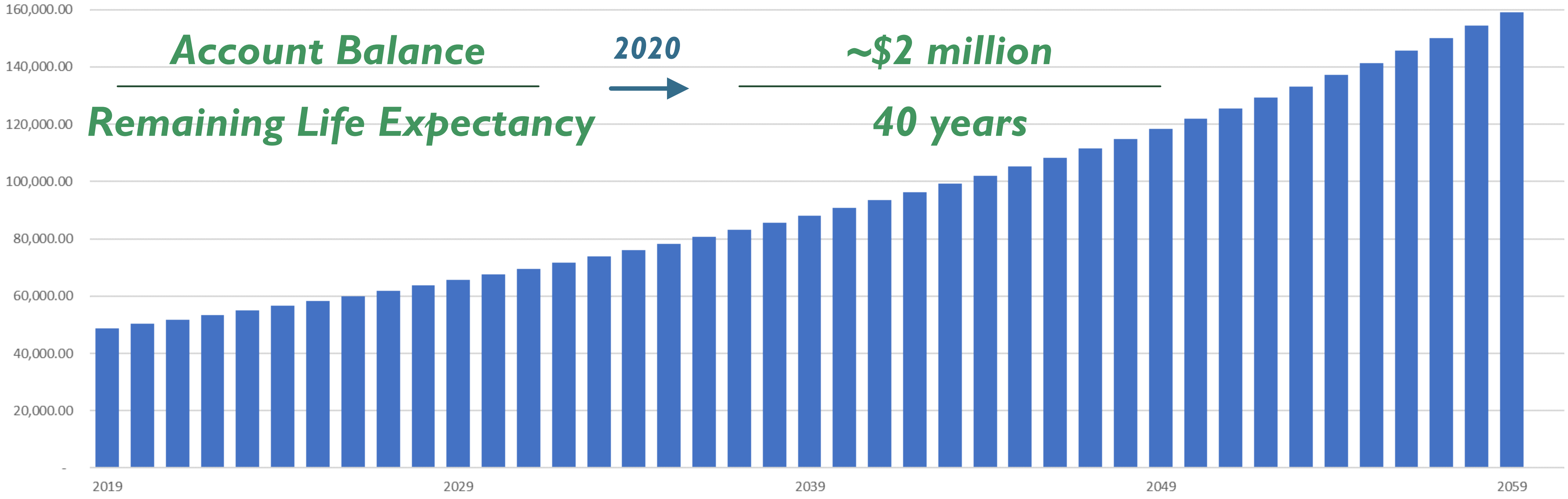
Beneficiary's Required Distributions – $2m IRA, 45-year-old son



41-year distribution period for 45-year-old

Blue = Required Distribution

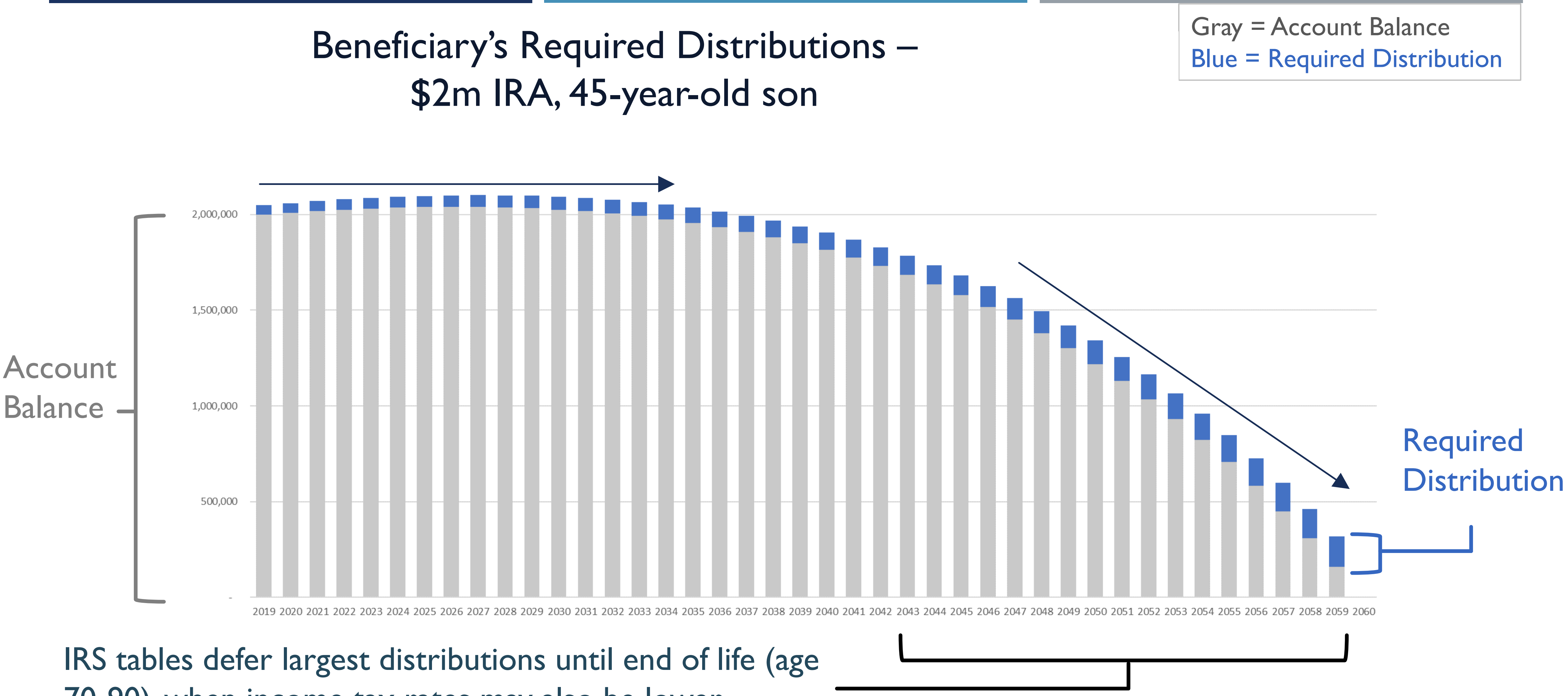
Beneficiary's Required Distributions – $2m IRA, 45-year-old son



41-year distribution period for 45-year-old

Pre-SECURE Act

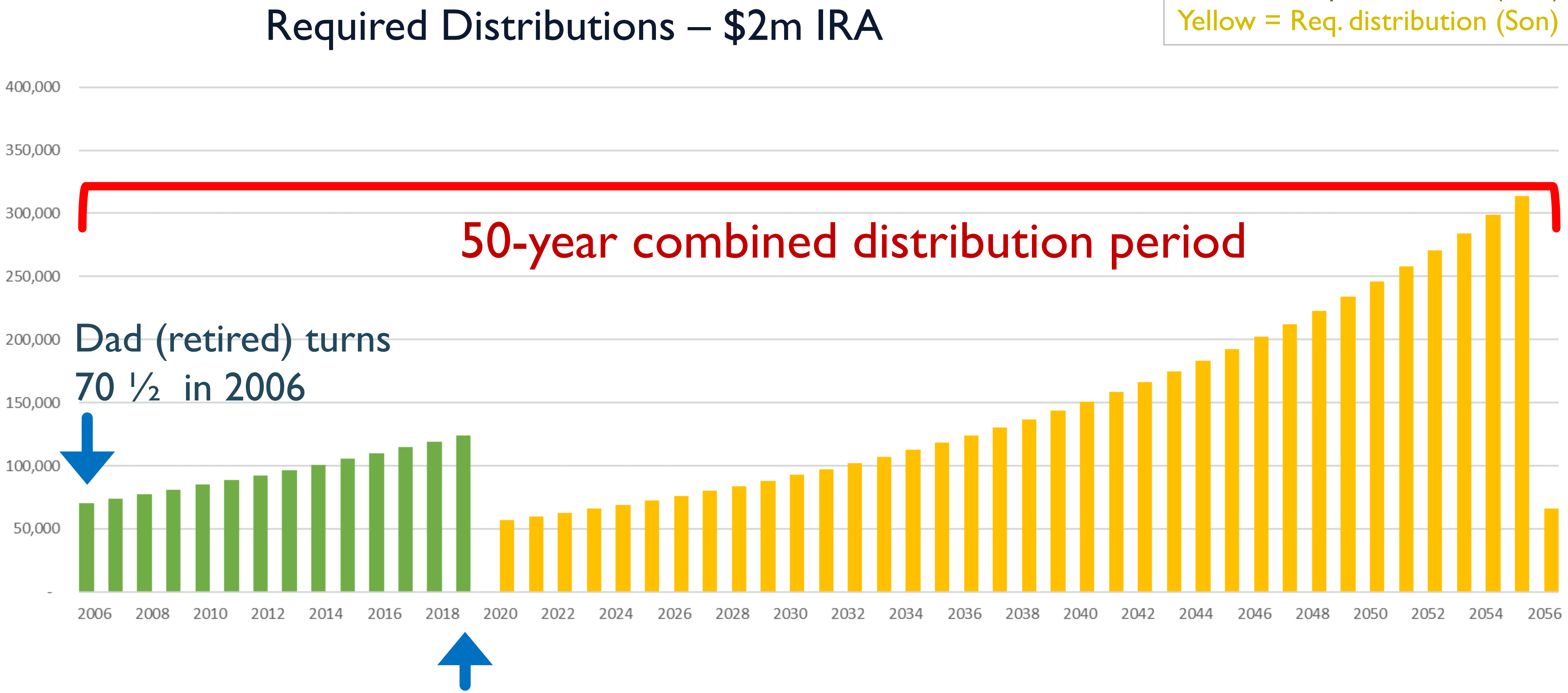
Beneficiary's Required Distributions – $2m IRA, 45-year-old son



IRS tables defer largest distributions until end of life (age 70-90), when income tax rates may also be lower

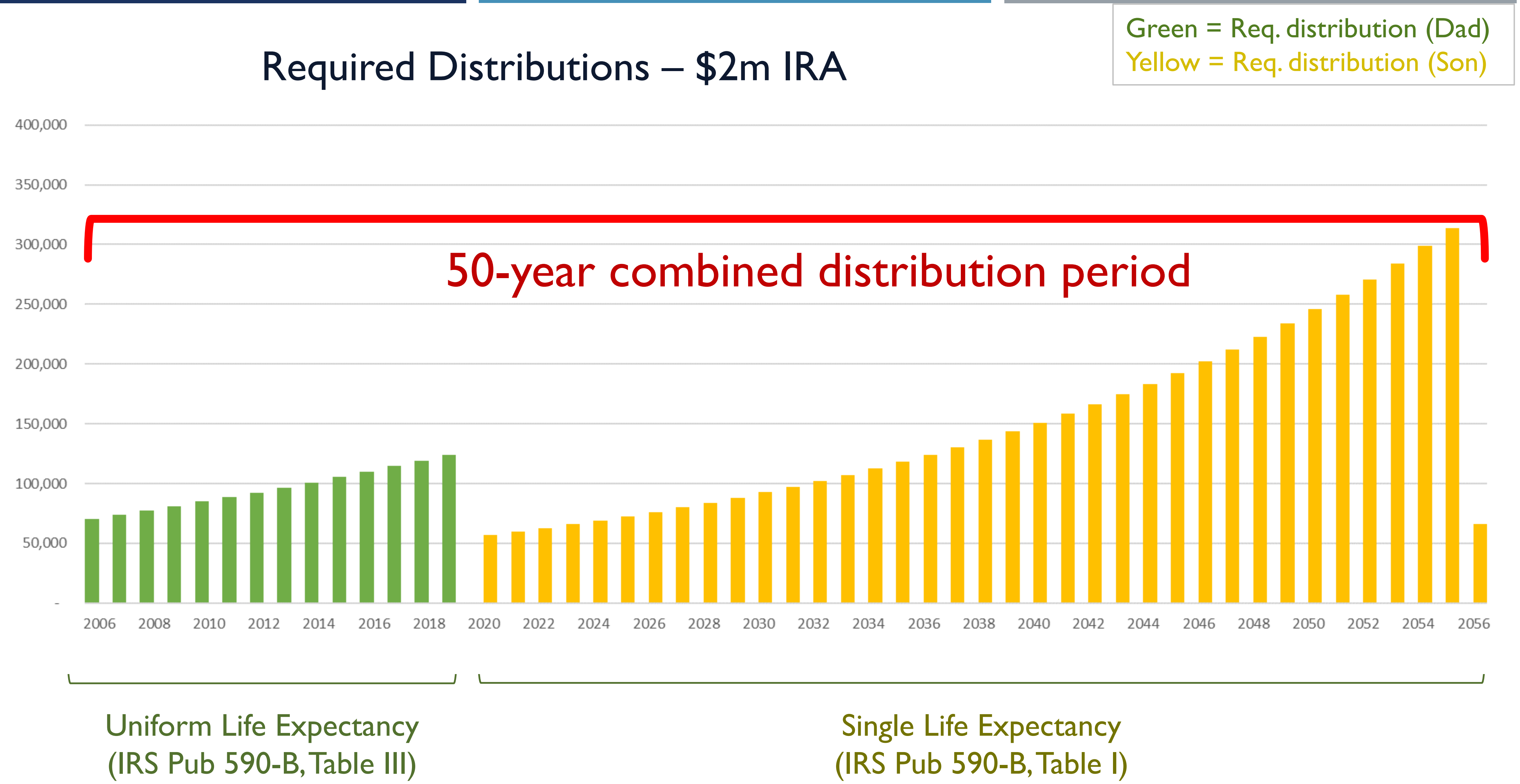
Pre-SECURE Act

Green = Req. distribution (Dad)
Yellow = Req. distribution (Son)



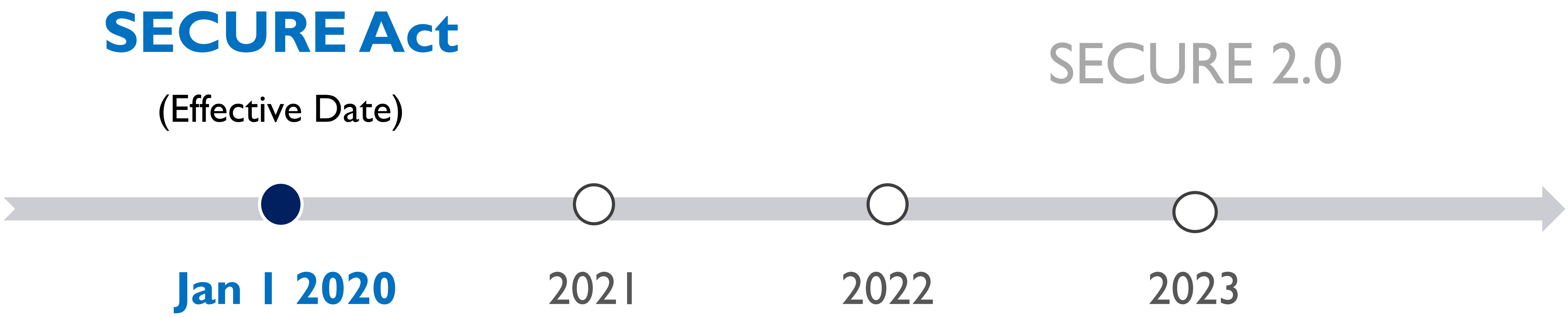
- Dad dies in 2019 (*age 84)*
- Son (age 50) is designated beneficiary of Dad's IRA

Required Distributions – $2m IRA



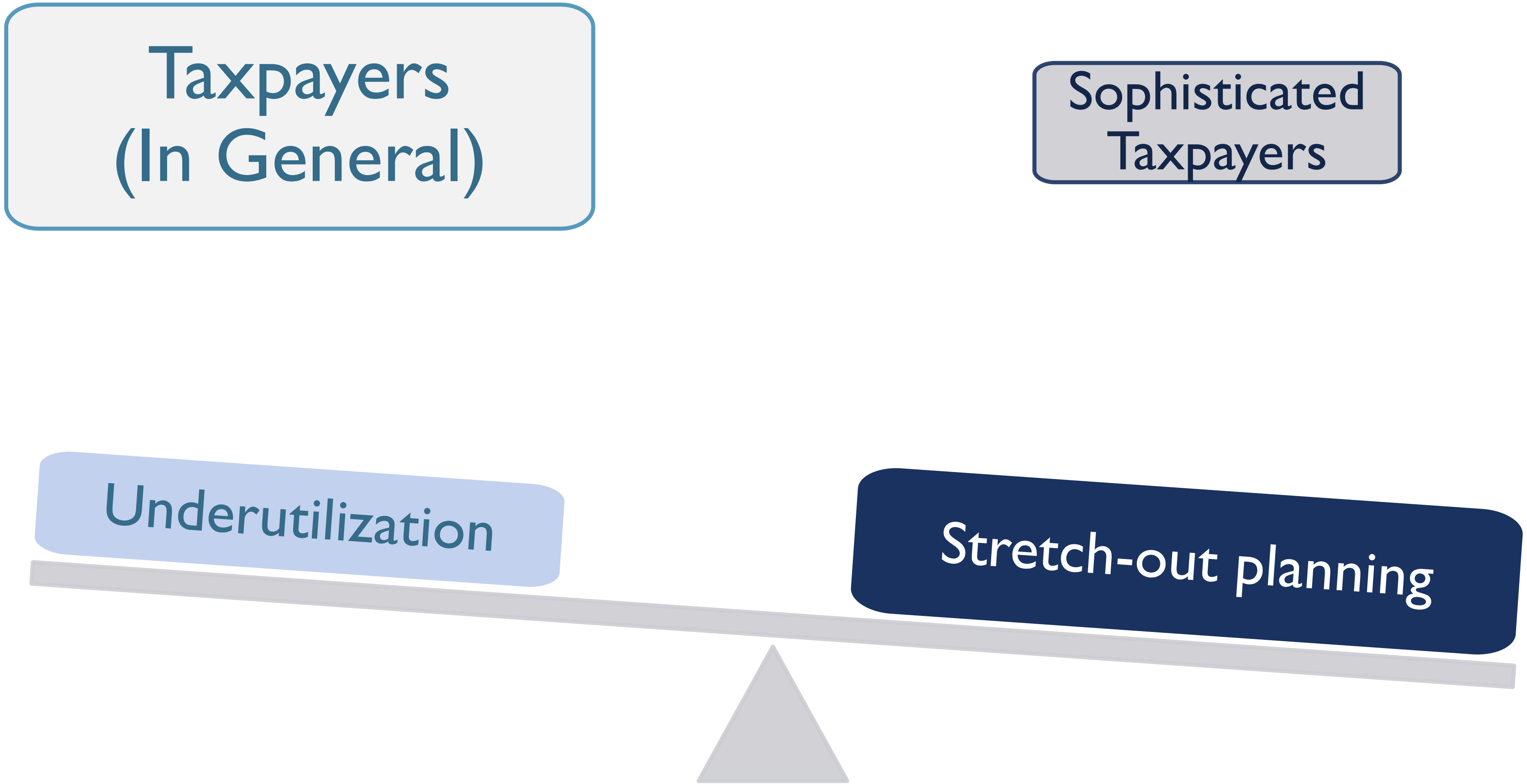
SECURE ACT OF 2019

"SETTING EVERY COMMUNITY UP FOR RETIREMENT ENHANCEMENT"



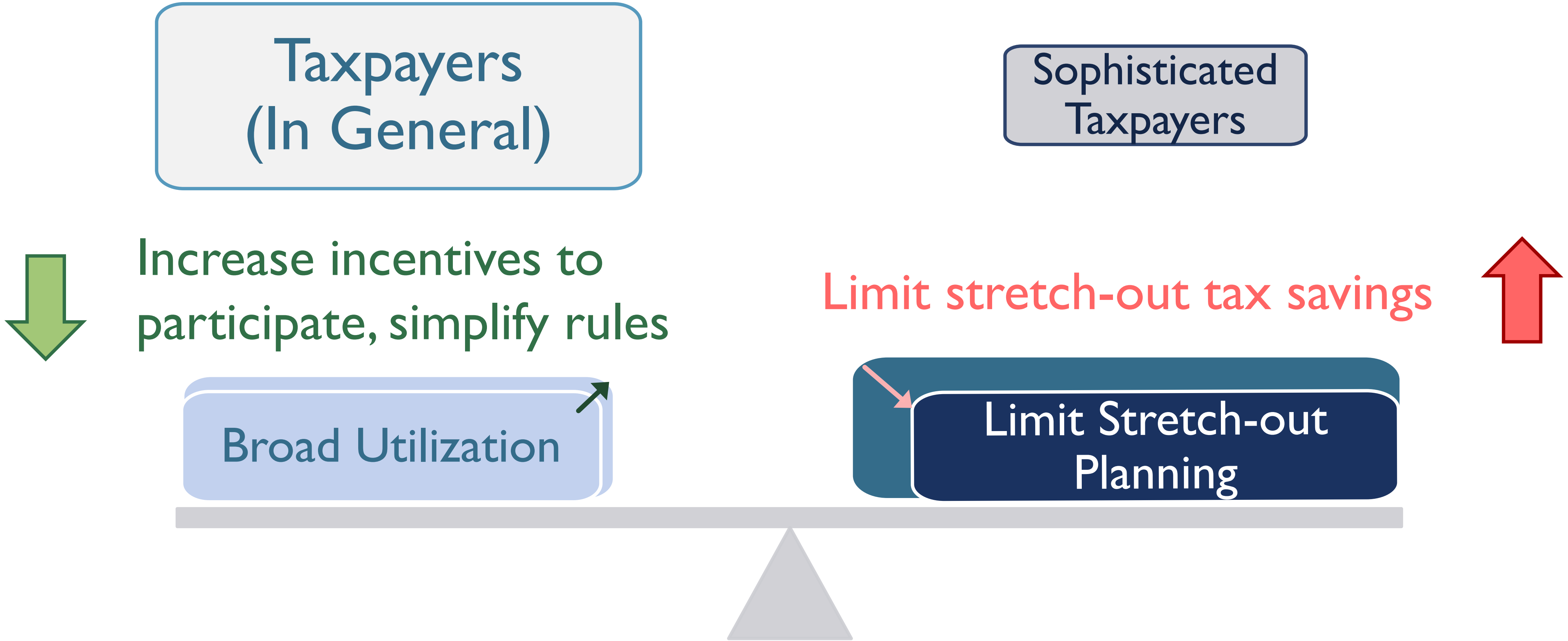
STATE OF RETIREMENT PLANNING (PRE-SECURE ACT)

DISPROPORTIONATE BENEFITS ACCRUED TO A MINORITY OF TAXPAYERS



CONGRESSIONAL INTENT

EXPAND AND EQUALIZE BENEFITS / FUND BY LIMITING STRETCH-OUT SAVINGS



SECURE ACT OF 2019

"SETTING EVERY COMMUNITY UP FOR RETIREMENT ENHANCEMENT"

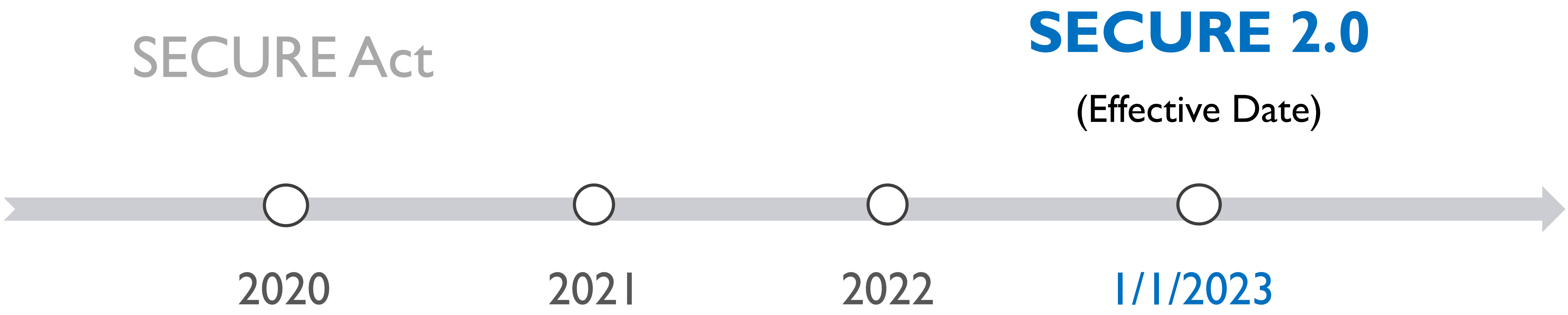
- Title I – "Expanding and Preserving Retirement Savings"
  - **Increases required beginning date from 70 ½ to 72**
  - Allows contributions after age 70 ½
  - Eases restrictions on multi-employer plans, enable part-time employees to participate in elective deferral plans, allow penalty-free distributions for births and adoptions, etc.
- Title IV – "Revenue Provisions"
  - **Establishes 10-year rule, limits stretch-out of required minimum distributions**
  - Increases penalties for failure to file, etc.

SECURE ACT OF 2019

"SETTING EVERY COMMUNITY UP FOR RETIREMENT ENHANCEMENT"

- ***Key Changes***
  - Increases required beginning date from 70 ½ to 72
  - Establishes10-year rule, limits stretch-out of required minimum distributions for many designated beneficiaries

SECURE 2.0 ACT OF 2022



SECURE 2.0 ACT OF 2022

- Title I
  - "Expand incentives for employers to offer retirement plans"
  - "Increase participation in employer-sponsored retirement plans"
  - "Increase the accumulation of savings in retirement plans""
    - ***Increased applicable age to 72 and 75 in two steps over 10 years***
- Title III
  - "Simplification and clarification of retirement plan rules"

SECURE 2.0 ACT OF 2022

- ***Key Change***
  - Increased applicable age to 72 and 75 in two steps over 10 years

REQUIRED DISTRIBUTION RULES (POST-SECURE 2.0)

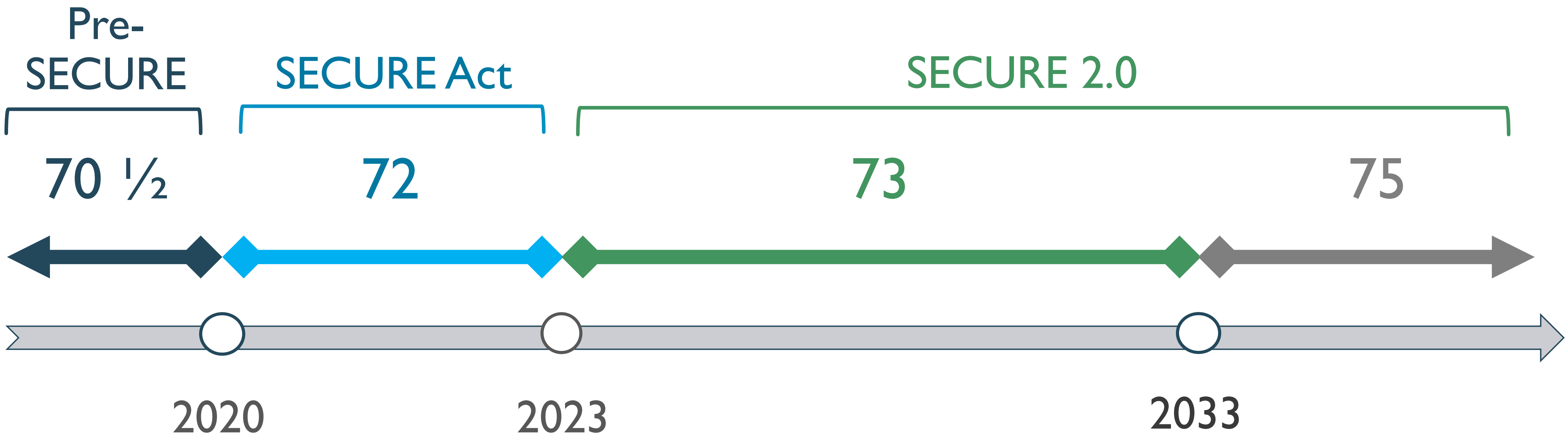
- Required Beginning Date
- Life Expectancy
- 10-Year Rule

REQUIRED BEGINNING DATE

- First distribution must be made on or before **April 1st** of the calendar year following the later of:
  - The calendar year in which the participant attains the **applicable age** or
  - The calendar year in which the participant **retires**

REQUIRED BEGINNING DATE

- Applicable Age



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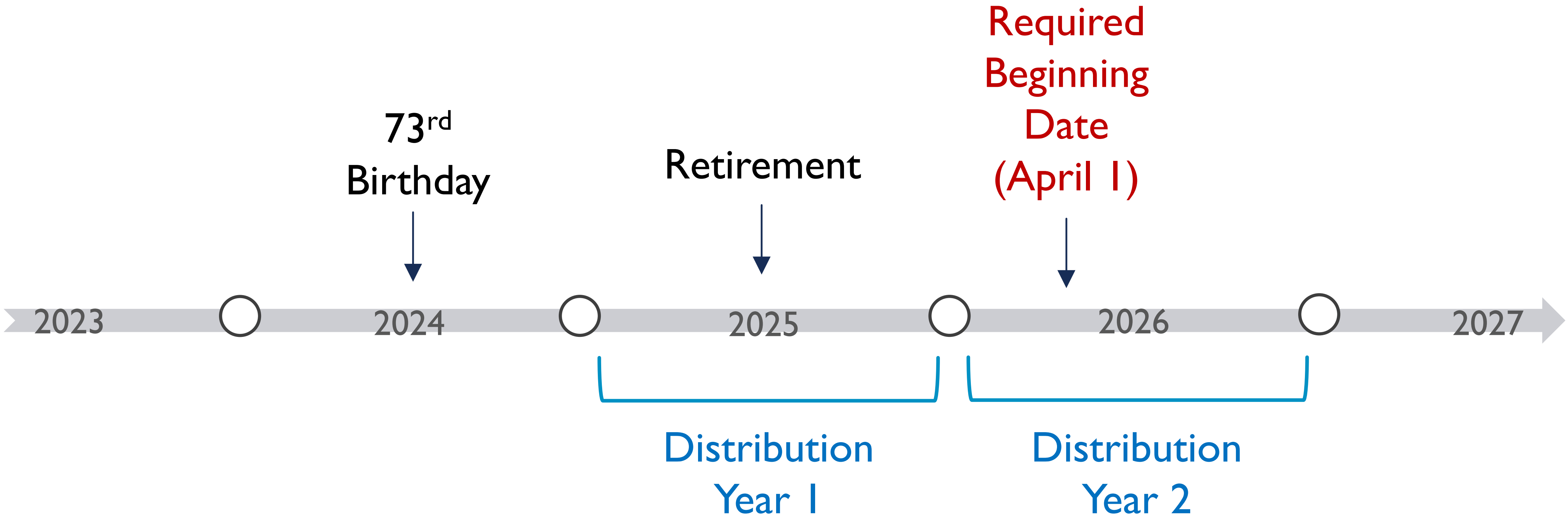

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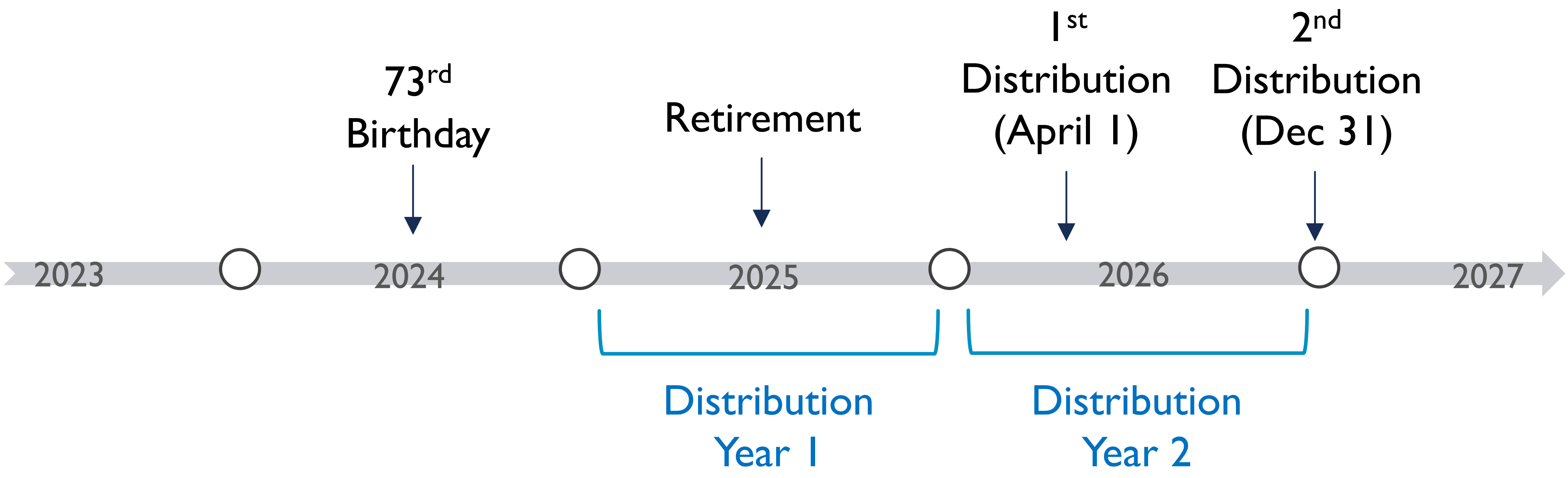
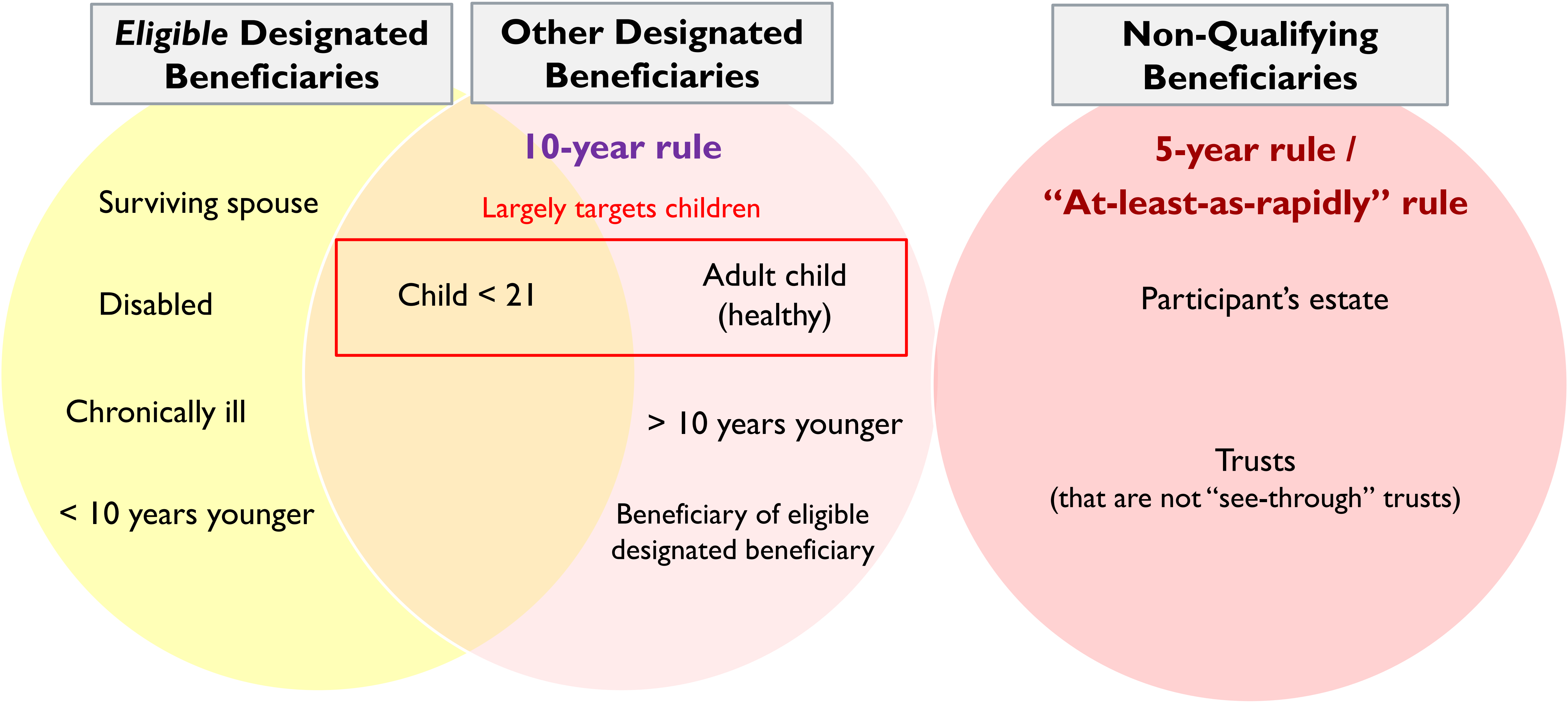


STRETCH-OUT PLANNING (POST-SECURE ACT)

- Only "**Eligible Designated Beneficiaries**" may stretch-out distributions for entire period of life expectancy
  - Spouse
  - Disabled/chronically ill
  - <10 years younger than participant
  - Minor children (must distribute entire account at ***age 31***)

10-YEAR RULE (POST-SECURE ACT)

- 10-year rule applies to **all *other* designated beneficiaries**
  - Participant's adult children (> age 21)
  - >10 years younger than participant
  - Beneficiaries of eligible designated beneficiary


Eligible Designated Beneficiaries
Other Designated Beneficiaries
Non-Qualifying Beneficiaries
10-year rule
Largely targets children
Surviving spouse
Disabled
Chronically ill
< 10 years younger
Child < 21
Adult child (healthy)
> 10 years younger
Beneficiary of eligible designated beneficiary
5-year rule /
"At-least-as-rapidly" rule
Participant's estate
Trusts
(that are not "see-through" trusts)

	Death *BEFORE* RBD	Death *AFTER* RBD
Eligible Designated Beneficiaries	Life expectancy (of beneficiary)	Life expectancy (of beneficiary)
Other Designated Beneficiaries	10-year rule *(deferred)*	10-year rule (annual life expectancy distributions)
Non-Qualifying Persons (Estates, Trusts)	5-year rule *(deferred)*	Life expectancy (of participant)

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Eligible Designated Beneficiaries	Life expectancy (of beneficiary)	Life expectancy (of beneficiary)
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Non-Qualifying Persons (Estates, Trusts)	5-year rule (deferred)	Life expectancy (of participant)

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Eligible Designated Beneficiaries	Life expectancy (of beneficiary)	Life expectancy (of ***beneficiary***)
Other Designated Beneficiaries	10-year rule (deferred)	10-year rule (annual life expectancy distributions)
Non-Qualifying Persons (Estates, Trusts)	5-year rule (deferred)	Life expectancy (of ***participant***)

At-least-as-rapidly rule
(Single Life, Table 1)

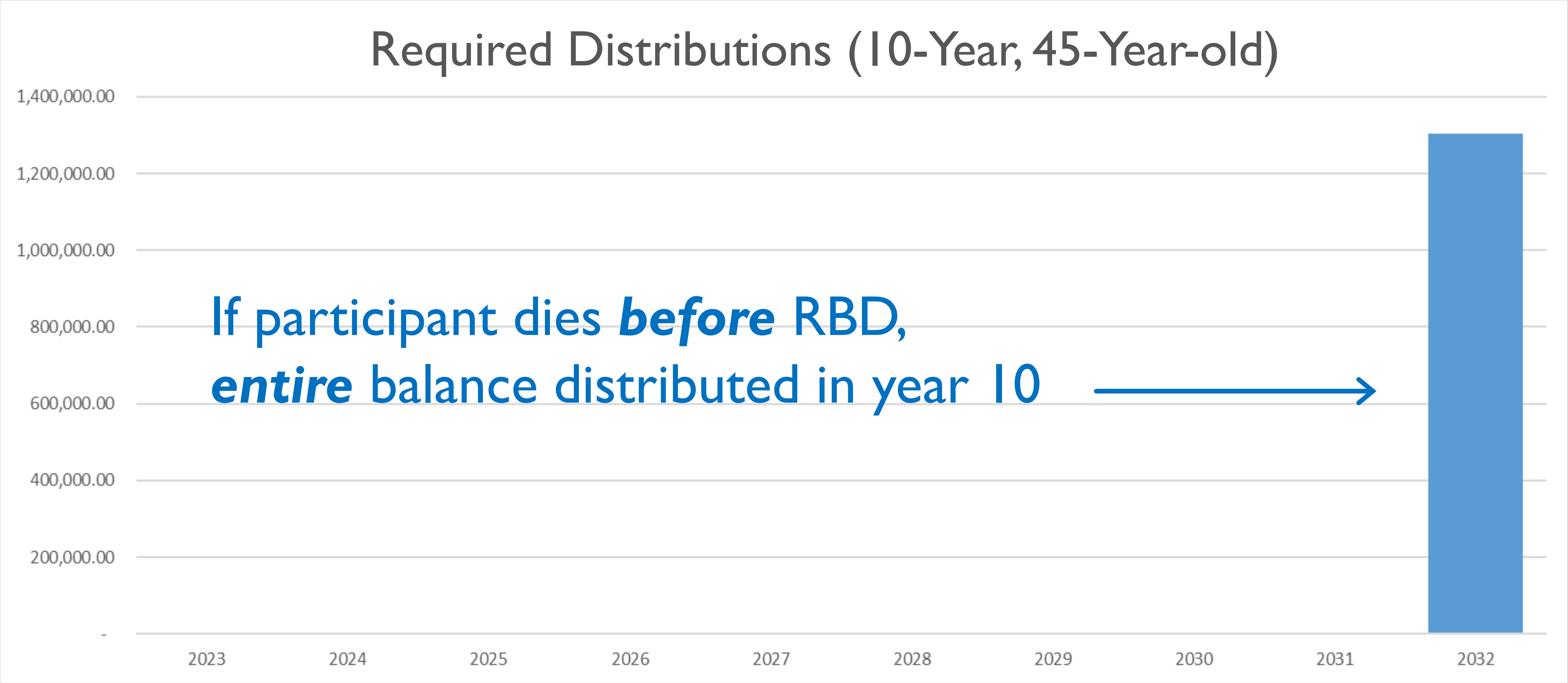
10-YEAR RULE

- Proposed Treasury Regulations
  - *Entire account balance* must be distributed before the end of the 10th year after participant's death (even if beneficiary dies during 10-year period)
    - If participant dies *before* RBD, then NO distributions required before 10th year
    - If participant dies *after* RBD, then annual distributions (based on beneficiary's life) must be made in years 1-9, with balance distributed in year 10.

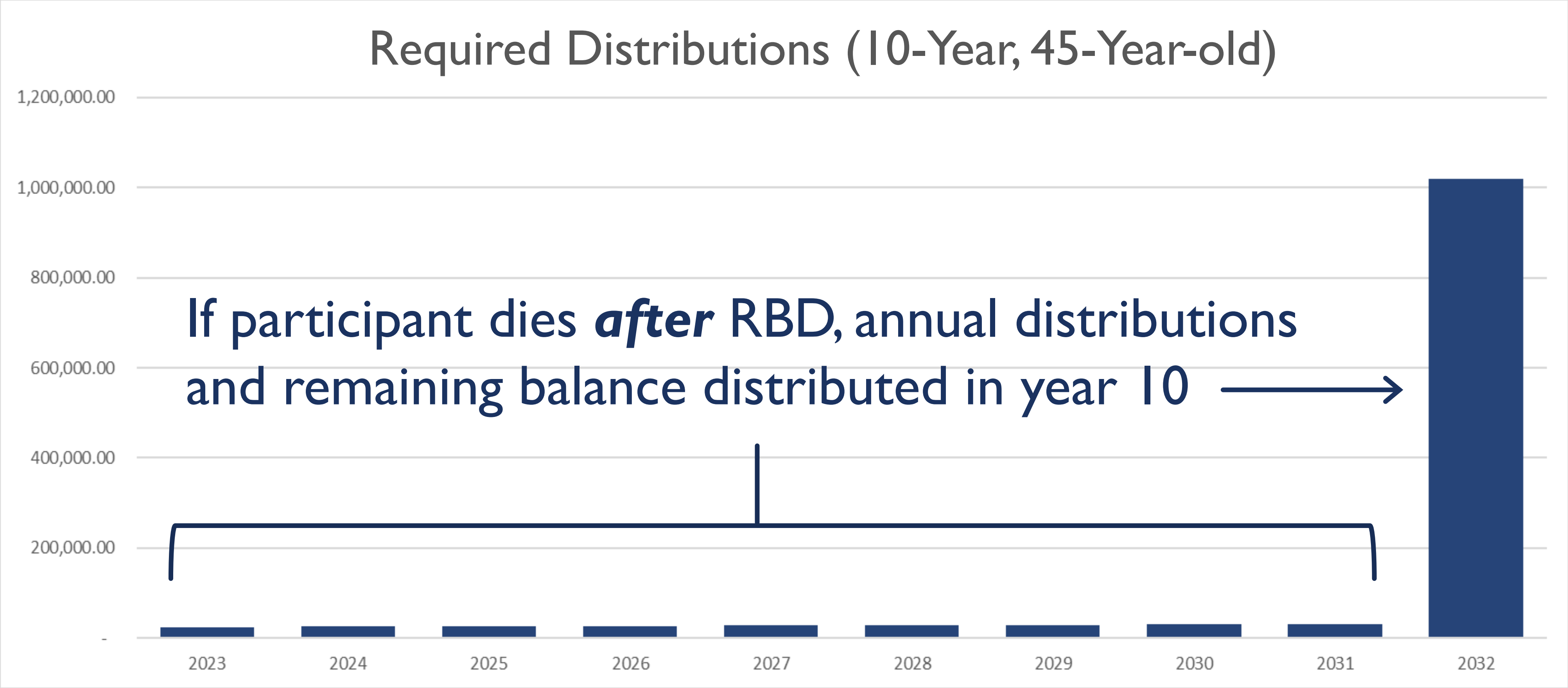
10-YEAR RULE

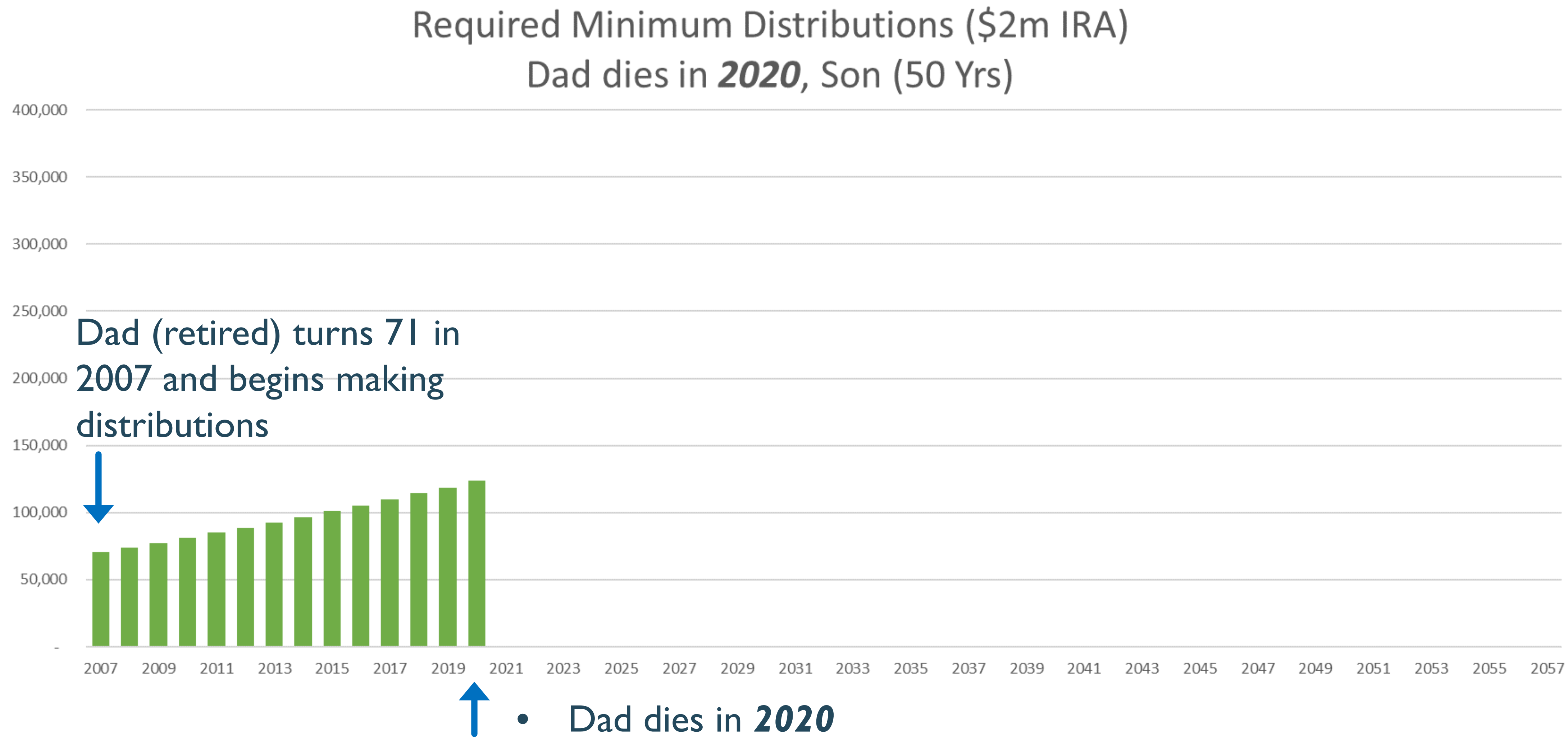
- Proposed Treasury Regulations
  - The proposed interpretation has been disputed by some commentators who argue that <u>deferral</u> is permitted under the statutory text—regardless of whether the participant died before the required beginning date
- IRS Notice 2023-54
  - IRS has granted a narrow safe harbor for distribution years 2021-2023
  - No penalty for failure to distribute required amount—applies only to beneficiaries subject to annual required distributions under the 10-year rule

10-Year Rule (Proposed Regulations)

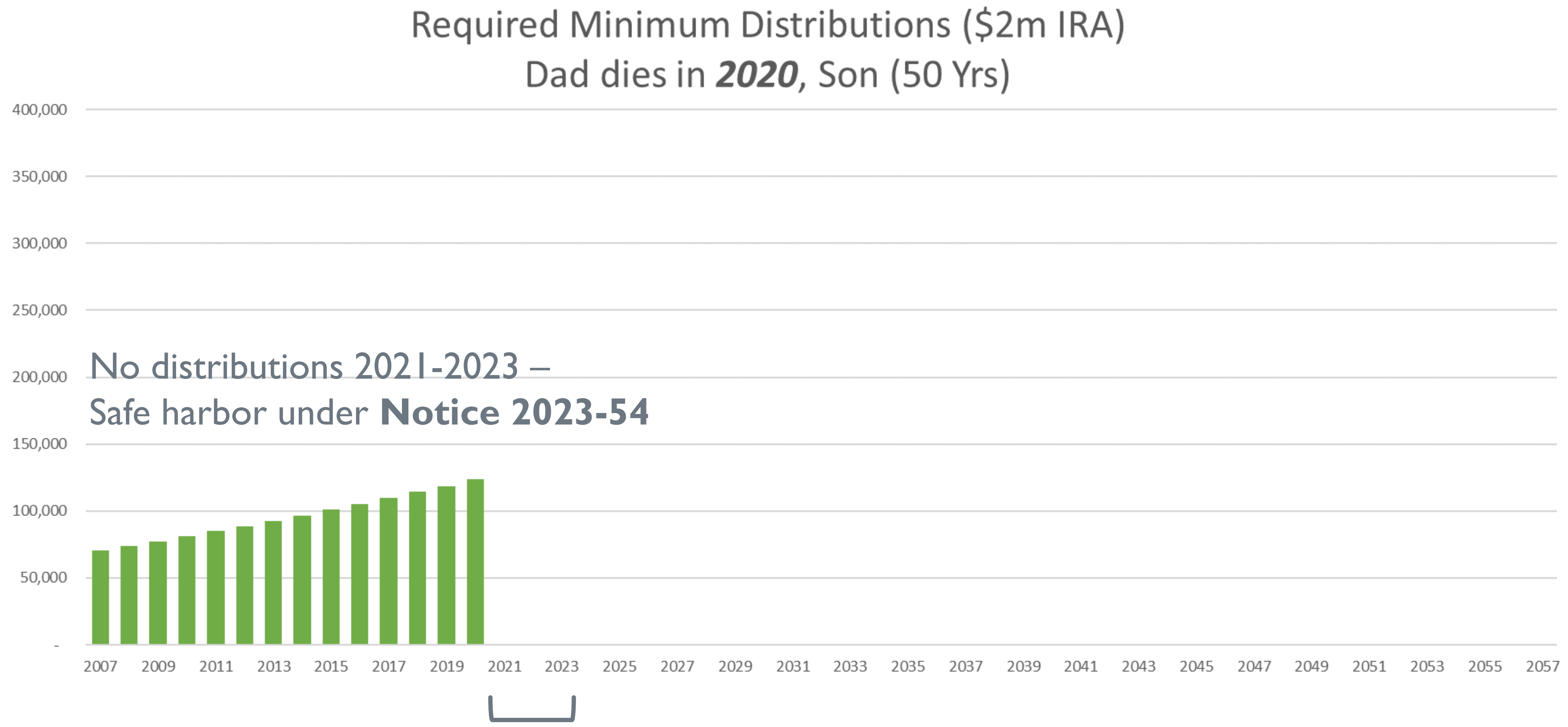


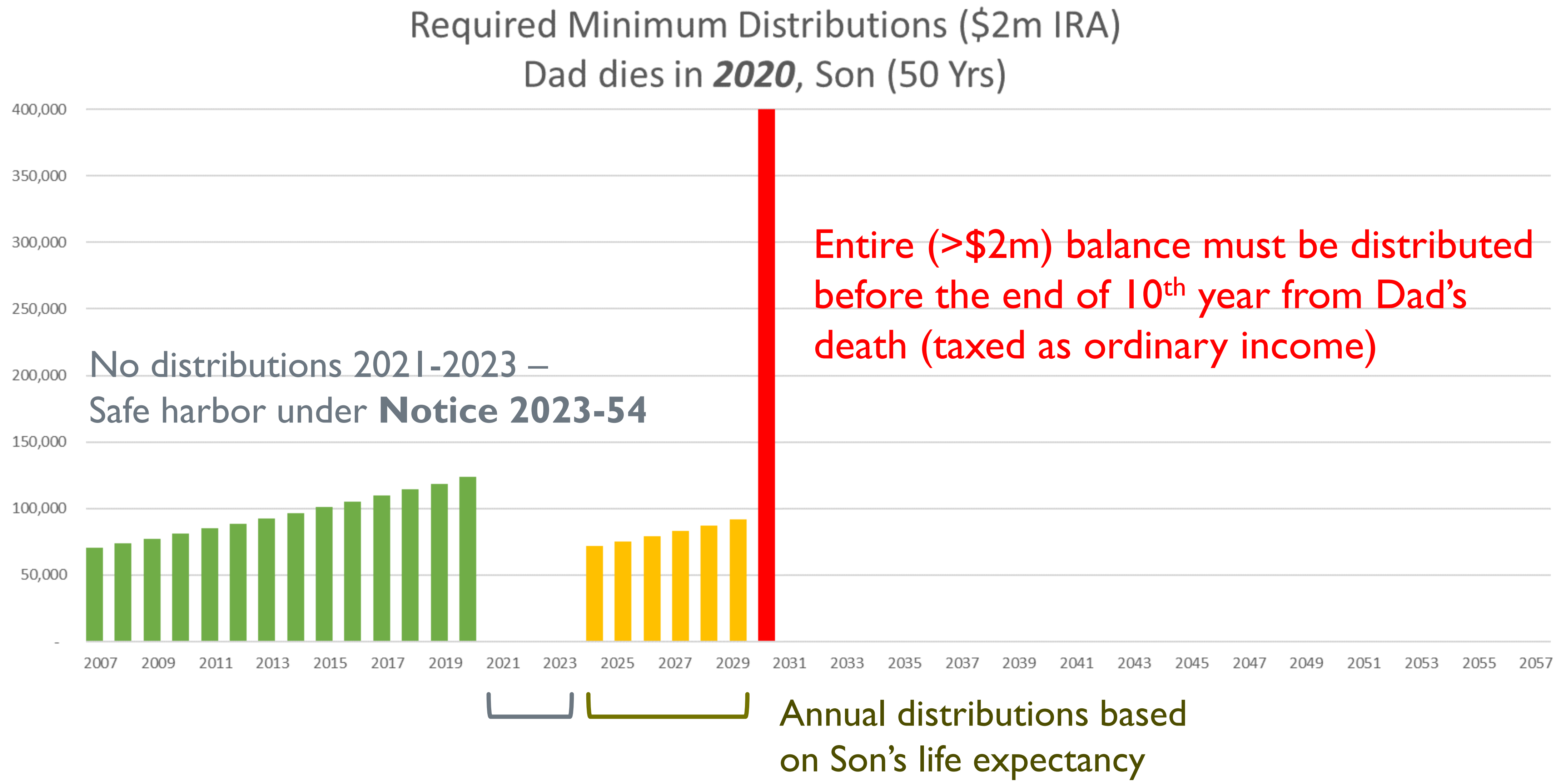
10-Year Rule (Proposed Regulations)





- Dad dies in ***2020***
- Son (50, healthy) is designated beneficiary of Dad's IRA


Required Minimum Distributions ($2m IRA)
Dad dies in 2020, Son (50 Yrs)
400,000
350,000
300,000
250,000
200,000
150,000
100,000
50,000
-
No distributions 2021-2023 –
Safe harbor under Notice 2023-54
2007 2009 2011 2013 2015 2017 2019 2021 2023 2025 2027 2029 2031 2033 2035 2037 2039 2041 2043 2045 2047 2049 2051 2053 2055 2057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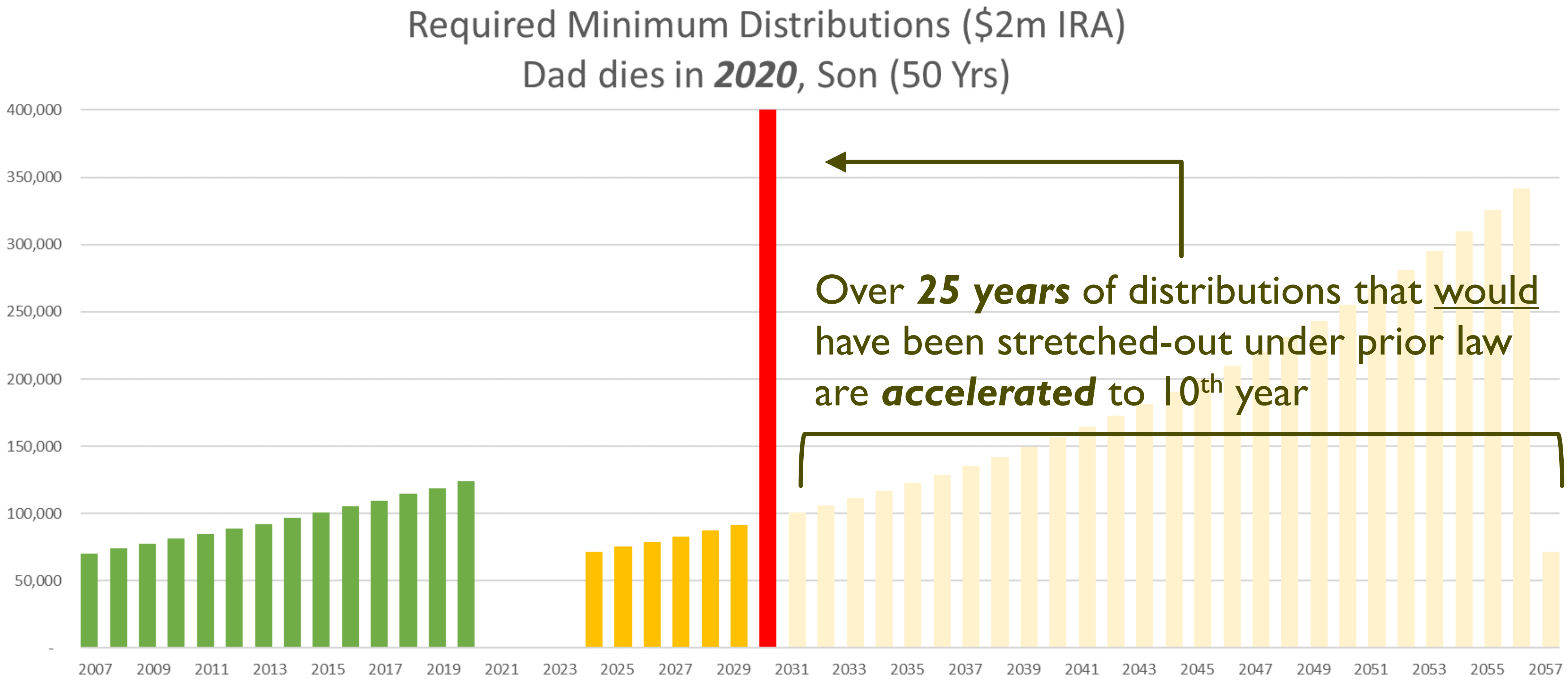
2057
No distributions 2021-2023 –
Safe harbor under **Notice 2023-54**
Entire (>$2m) balance must be distributed before the end of 10th year from Dad's death (taxed as ordinary income)
Annual distributions based on Son's life expectancy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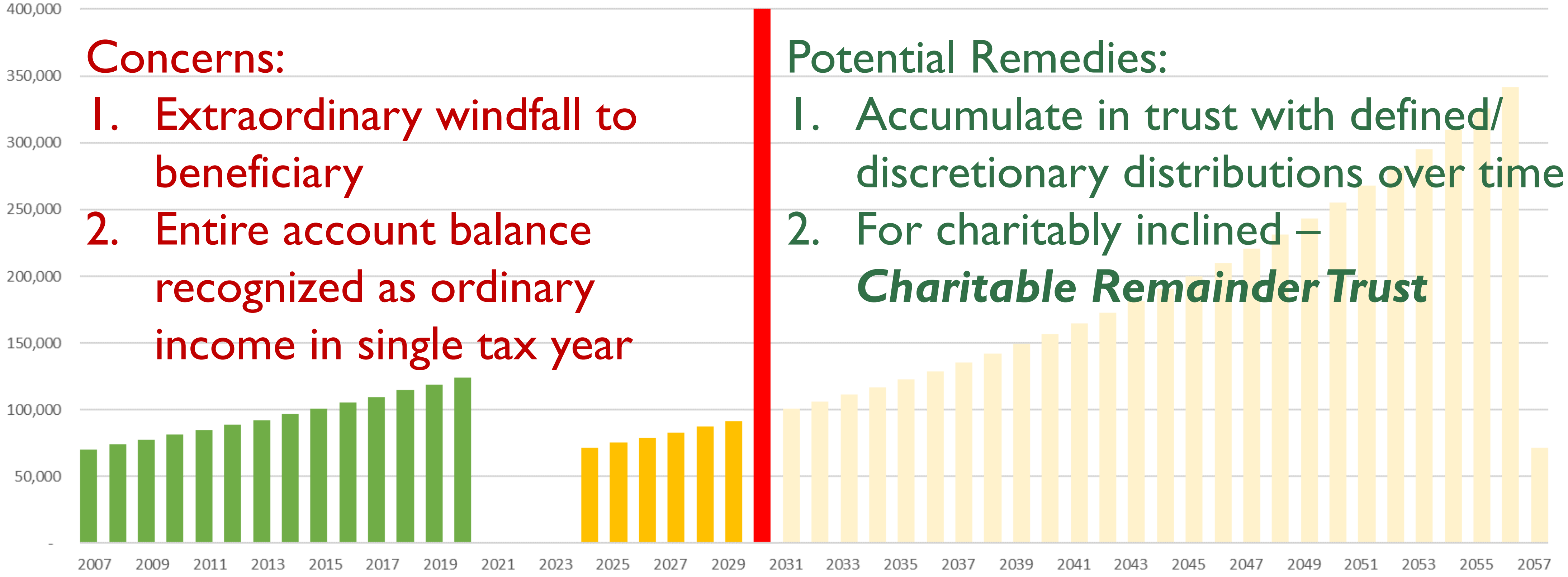
2007 2009 2011 2013 2015 2017 2019 2021 2023 2025 2027 2029 2031 2033 2035 2037 2039 2041 2043 2045 2047 2049 2051 2053 2055 2057
Over **25 years** of distributions that would have been stretched-out under prior law are ***accelerated*** to 10th year

Required Minimum Distributions ($2m IRA)
Dad dies in ***2020***, Son (50 Yrs)



Concerns:

1. Extraordinary windfall to beneficiary
2. Entire account balance recognized as ordinary income in single tax year

Potential Remedies:

1. Accumulate in trust with defined/ discretionary distributions over time
2. For charitably inclined – ***Charitable Remainder Trust***

Trusts as Plan Beneficiaries

- GENERAL RULE
  - Trusts do <u>not</u> qualify as designated beneficiaries, **5-year rule** or **"at-least-as-rapidly" rule** applies
- EXCEPTION
  - If the trust qualifies as a "**see-through trust**," then *look through the trust* to determine the plan beneficiaries (and required distributions)
    - Eligible designated beneficiaries – annual life expectancy distributions
    - Other designated beneficiaries – 10-year rule

See-Through Trust

1. The trust must be **valid under state law** (or would be except that there is no trust corpus)
2. Trust is **irrevocable** or will become irrevocable upon death of participant
3. The trust beneficiaries (with respect to the retirement plan) are **identifiable**
4. Requisite **documentation** is timely provided to the plan trustee

See-Through Trust

- Trust beneficiaries are treated as ***PLAN beneficiaries*** if –

1. The trust beneficiary can receive distributions representing the employee's interest in the retirement plan
2. The distributions are not contingent on the death of another beneficiary

- **See-Through Trust**
  - **Conduit Trust**
    - Terms ***prohibit* accumulation** of plan distributions
  - **Accumulation Trust**
    - Terms ***allow* accumulation** of plan distributions

Conduit Trust

Tier 1 – Plan Beneficiary

- All plan distributions **MUST** be paid to/for specified beneficiaries

Tier 2 – Not a Plan Beneficiary

- Beneficiary may **ONLY** receive payments representing the participant's interest in the plan after the death of a Tier 1 Beneficiary

Accumulation Trust

Tier 1 – Plan Beneficiary

- Plan distributions **MAY** be paid to/for specified beneficiaries *or may be accumulated*

Tier 2 – Plan Beneficiary

- After death of Tier 1 beneficiary, Tier 2 beneficiary **MAY** receive distributions representing the participant's interest in the plan that were accumulated, i.e., not distributed to Tier 1 Beneficiaries

Tier 3 – Disregarded Beneficiary

- Beneficiary may **ONLY** receive payments representing the participant's interest in the plan after the death of a Tier 2 Beneficiary

Conduit Trust	Accumulation Trust
Tier 1 – Plan Beneficiary	**Tier 1** – Plan Beneficiary
Tier 2 – <u>Not</u> a Plan Beneficiary	**Tier 2** – Plan Beneficiary
	Tier 3 – Disregarded Beneficiary

If (e.g.) charity is considered to be a plan beneficiary, then the **5-year / at-least-as-rapidly rules** apply

Conduit Trust

Tier 1 – Plan Beneficiary

Tier 2 – Not a Plan Beneficiary

Accumulation Trust

Tier 1 – Plan Beneficiary

Tier 2 – Plan Beneficiary

Tier 3 – Disregarded Beneficiary

If (e.g.) charity is not a plan beneficiary (or is disregarded) then the distribution period is determined based on the designated beneficiaries and **life expectancy** or the **10-year rule** will apply.

CHARITABLE PLANNING WITH RETIREMENT ACCOUNTS

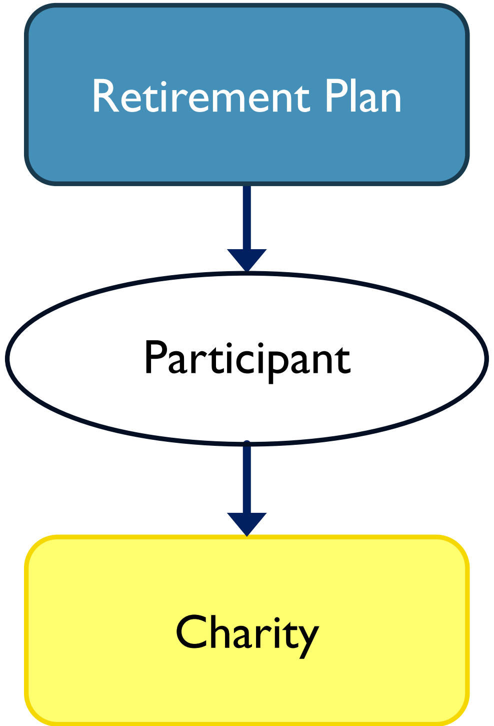
- Basic Strategies
  1. Deductible charitable contribution (after taxable distribution)
  2. Qualified charitable distribution (“QCD”)
  3. Outright testamentary distribution to charity
  4. Trust or estate disposition to charity
  5. Charitable gift annuity (“CGA”)
  6. Charitable remainder trust (“CRT”)

1. DEDUCTIBLE CHARITABLE CONTRIBUTION

I. DEDUCTIBLE CHARITABLE CONTRIBUTION

Required distribution—
included in gross income

Charitable contribution deduction—
subject to 60/50/30/20% AGI limitations
(may be carried forward 5 years)



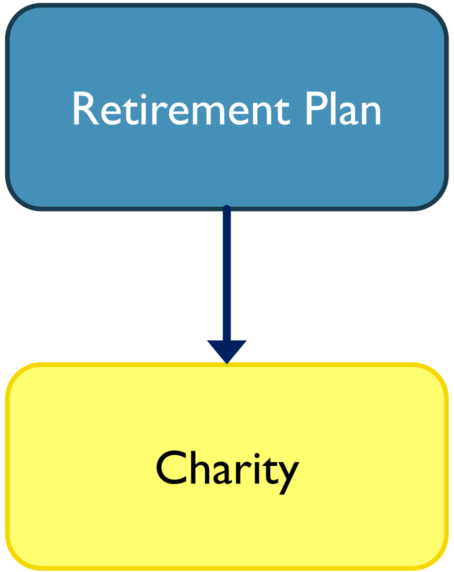
2. QUALIFIED CHARITABLE DISTRIBUTION

- **Why consider it?** If made directly by the plan trustee to a qualifying charity, up to $100,000 of charitable distributions may be *counted* towards required minimum distribution and *excluded from gross income*
  - Potentially $200,000 for married couple (i.e., $100,000 from *each* spouse's plan)
  - No 60%, 50%, 30%, 20% limitations on charitable deduction apply

2. QUALIFIED CHARITABLE DISTRIBUTION

Qualified charitable distribution—

1. ***excluded from gross income****, and*
2. ***counts against required distribution***



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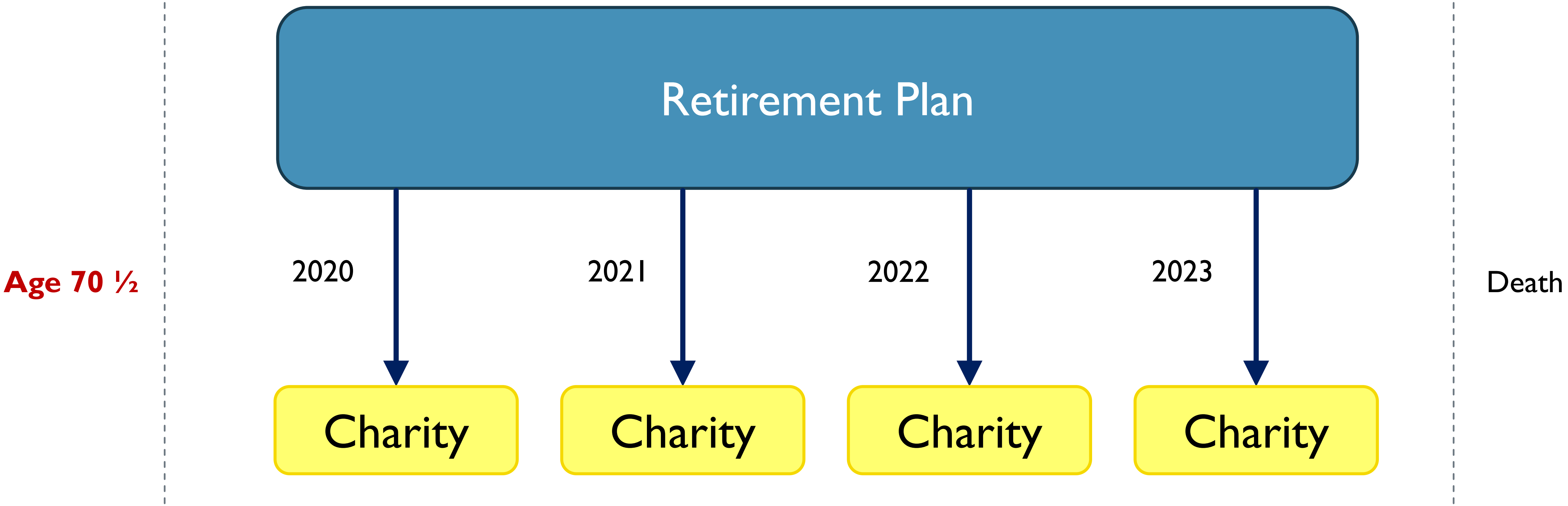


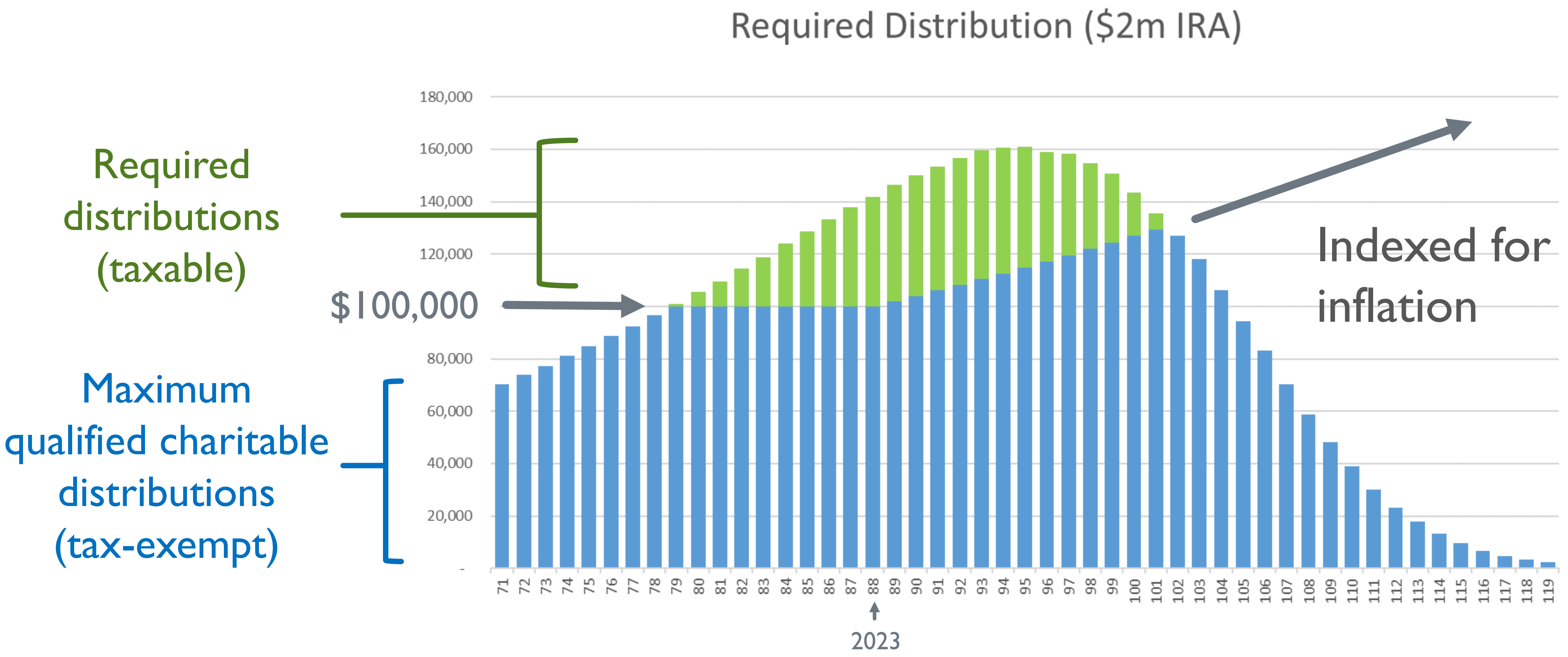
2. QUALIFIED CHARITABLE DISTRIBUTION

- **Basic Requirements:**
  - Must be **70 ½** years or older (*no longer corresponds to required beginning date*)
  - Qualifying Charity:
    - Includes Charitable Split-Interest Entity
    - Does not include donor advised fund (DAF)
    - Limitations apply for charities over which donor may exercise control or discretion
  - Must receive contemporaneous written acknowledgment from charity (IRC §170(f)(8))

2. QUALIFIED CHARITABLE DISTRIBUTION

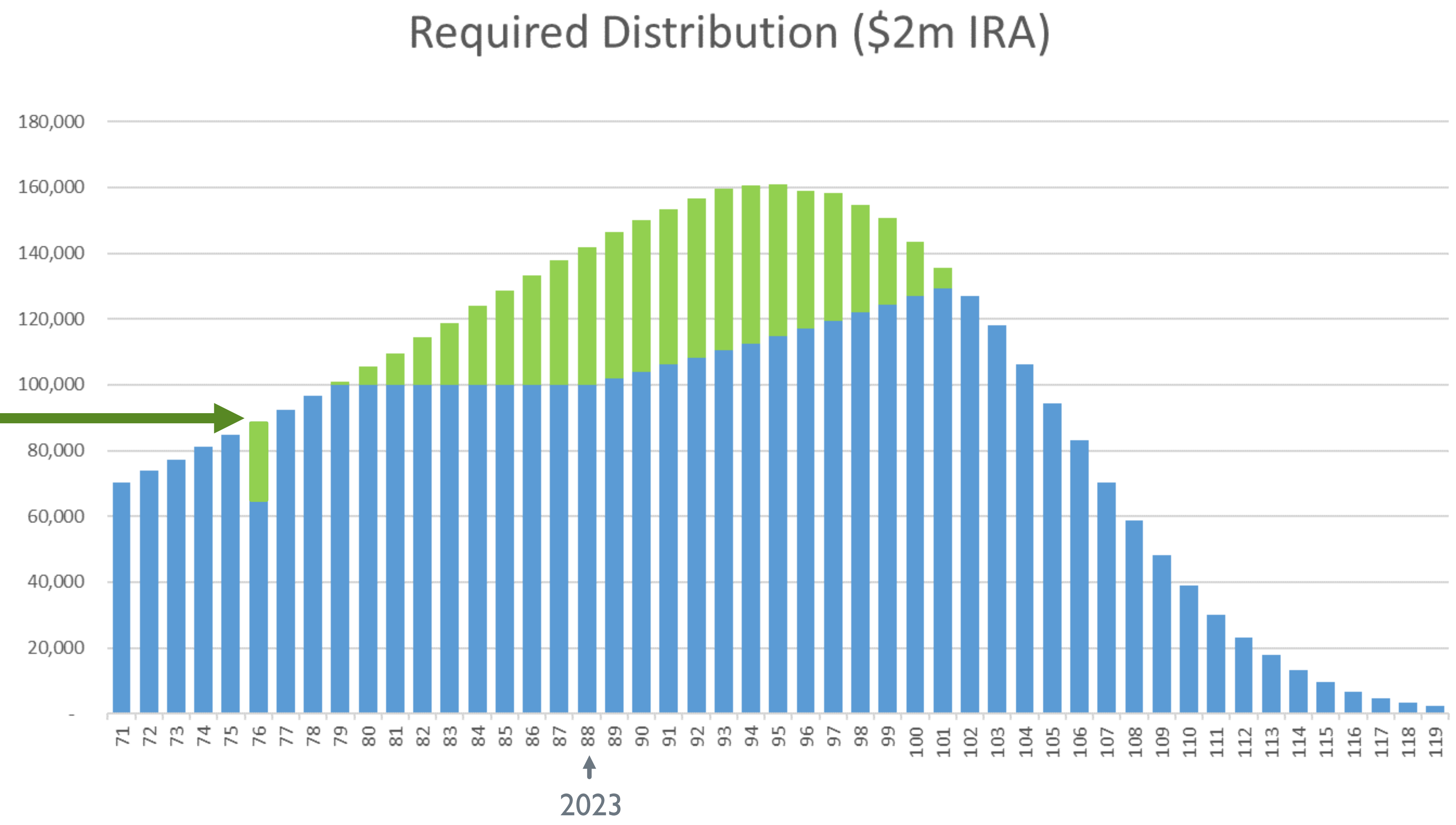
- **Maximum QCD:**
  - $100,000 maximum indexed for inflation under SECURE 2.0 (beginning in 2024)
  - Maximum annual amount reduced dollar-for-dollar by deductible plan contributions after age 70 ½ (unless contribution was previously applied to reduce a QCD in a prior year)

Qualified Charitable Distributions



Qualified Charitable Distributions

$20,000 deductible contribution at age 75 reduces QCD dollar-for-dollar in following calendar year



Qualified Charitable Distributions

Married Couple (both over 70 ½, separate IRAs)	**Charitable Contribution Deduction**	**Qualified Charitable Distribution**
Required Distribution (IRA)	$200,000	$200,000
Qualified Charitable Distribution	$0	($200,000)
IRA Distribution Received	$200,000	$0
Other Income	$60,000	$60,000
AGI	260,000	$60,000
Charitable Contribution	$200,000	$0
Contributed Assets	Cash	N/A
Charitable Contribution Deduction	($156,000)	$0
Standard Deduction	$0	($26,000)
Taxable Income	$104,000	$34,000
Approximate Federal Income Tax	$25,000	$8,250

Distributed directly to charity, ***excluded*** from gross income

Cash distribution subject to applicable 60% deduction limitations

$16,750 Difference

2. QUALIFIED CHARITABLE DISTRIBUTION

- **Gift to Charitable Split Interest Entities**
  - Charitable Gift Annuity (CGA)
  - Charitable Remainder Trust (CRT)

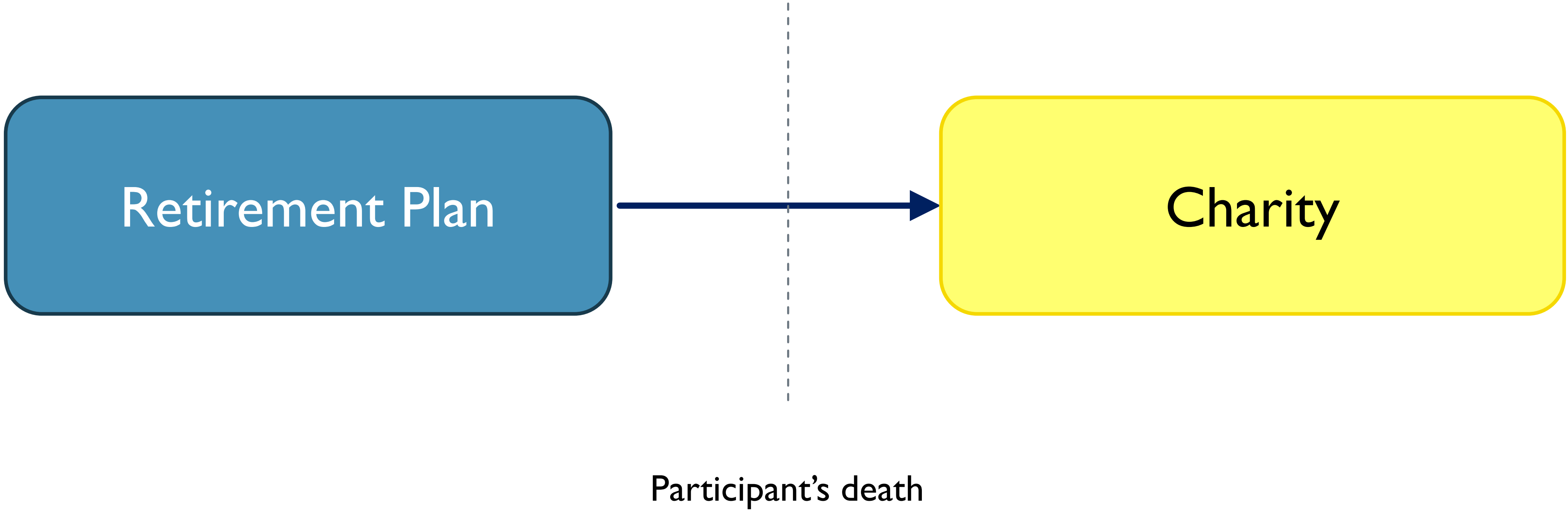
2. QUALIFIED CHARITABLE DISTRIBUTION

- **Gift to Charitable Split Interest Entities**
  - **One-time only, limited to $50,000**
  - Qualifying CGA or CRT may only hold QCD distributions (may not be commingled with other assets)
  - Only participant (and spouse) may be a beneficiary
  - Income interest to non-charitable beneficiary is not transferable
  - Generally, distributions from a Charitable Split Interest Entity are taxed as ordinary income

2. QUALIFIED CHARITABLE DISTRIBUTION

- **Gift to Charitable Split Interest Entities**
  - **Economic viability of one-time $50,000 QCD**
  - It may make more sense to distribute to CGA than to a CRT
    - CGA is a contract that is fully administered by the charity
    - CRT is privately set up and administered at the donor's expense
    - Non-assignability of income interest may conflict with state law creditor rights
    - $50,000 maximum may be below threshold for "non-economical trust"
      - See Calif. Probate Code 15408

3. OUTRIGHT DISTRIBUTIONS TO CHARITY ON PARTICIPANT'S DEATH



3. OUTRIGHT DISTRIBUTIONS TO CHARITY ON PARTICIPANT'S DEATH

- **Why?**
  - **Genuine charitable intent**
  - **Tax efficient**
    - Unlimited estate tax charitable deduction
    - Income tax free (because charity is tax exempt)

3. OUTRIGHT DISTRIBUTIONS TO CHARITY ON PARTICIPANT'S DEATH

- **How?**
  - Beneficiary designation form
    - **Best practice:** Contact charity first to request suggested language

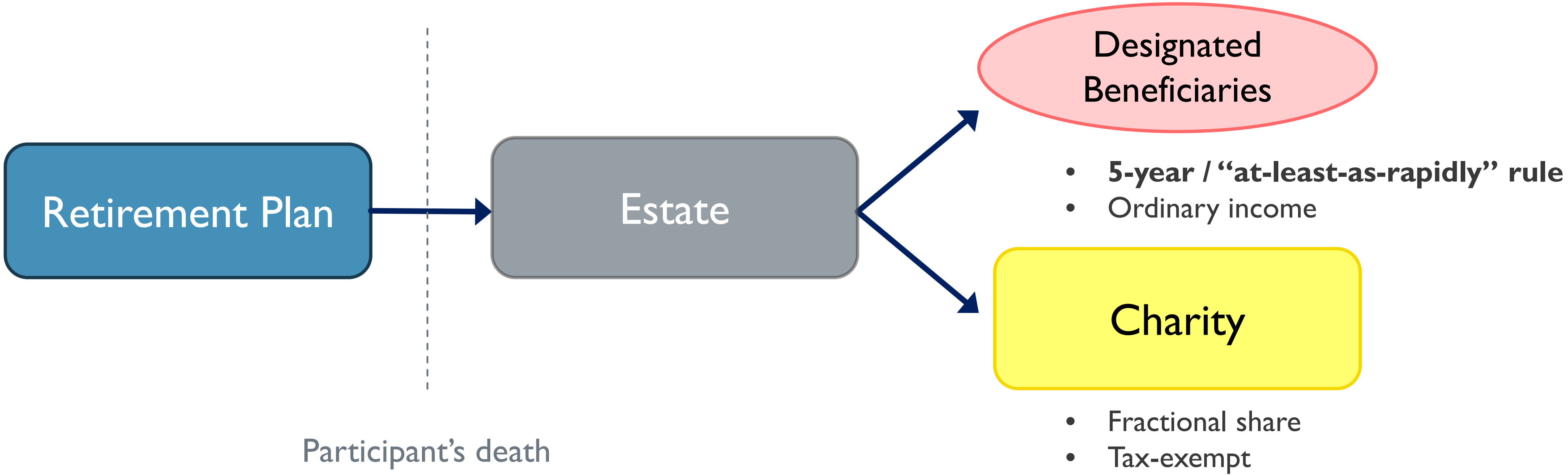
3. OUTRIGHT DISTRIBUTIONS TO CHARITY ON PARTICIPANT'S DEATH

- **How?**
  - Timely distributions
    - PROBLEM: Charity may defeat stretch-out benefits for designated beneficiaries (by triggering the 5-year rule or "at-least-as-rapidly" rule)
    - REMEDY: Charity is <u>not</u> considered for RMD purposes ***if*** entire interest is distributed by September 30 of the calendar year following the calendar year of the participant's death

3. OUTRIGHT DISTRIBUTIONS TO CHARITY ON PARTICIPANT'S DEATH

- **CAUTION**
  - Charitable designations must be certain and ascertainable to qualify for a deduction
    - See Treas. Reg. §20.2055-2
  - Estate plan should ensure estate taxes are not allocated to charitable gift (by will/trust terms or by state law) otherwise amount intended for charity is reduced
  - Plan administrators—who are wary of being subject to fiduciary legal standards—may balk at formulas that are overly complex or that involve family relationships or individual behavior
  - Disclaimer may be invalid if proceeds are allocated to a charity over which the disclaimant exercises control or discretion

4. TRUST OR ESTATE DISPOSITION TO CHARITY



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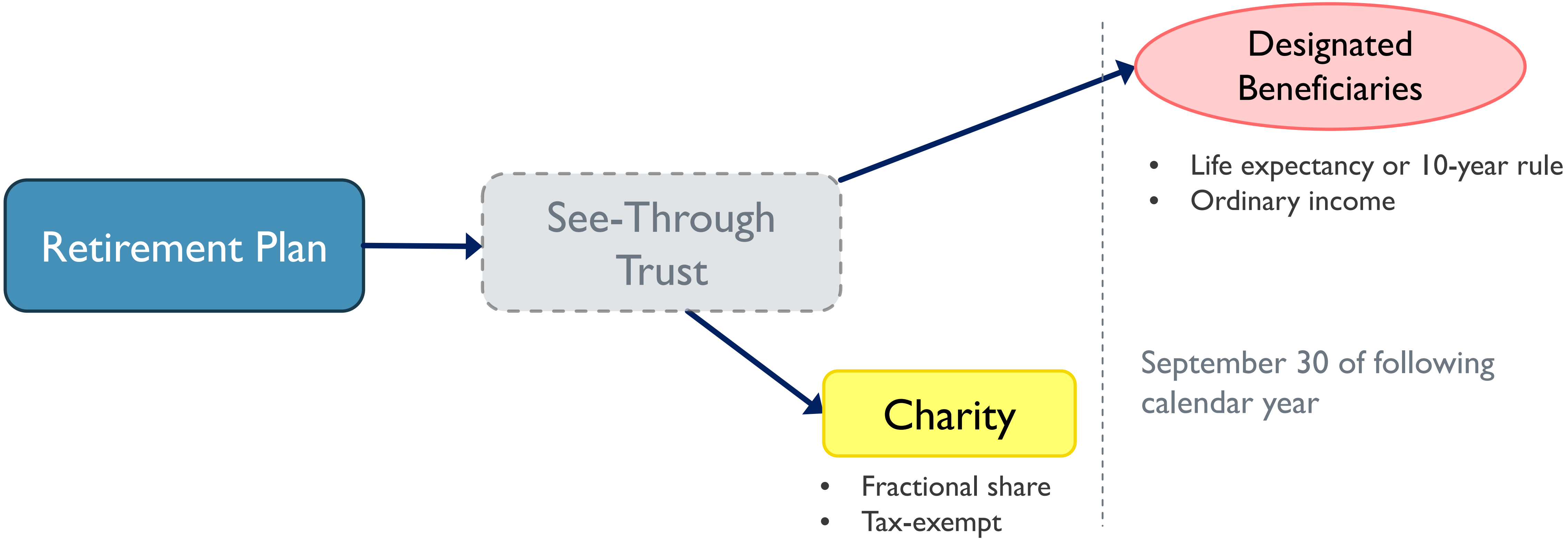
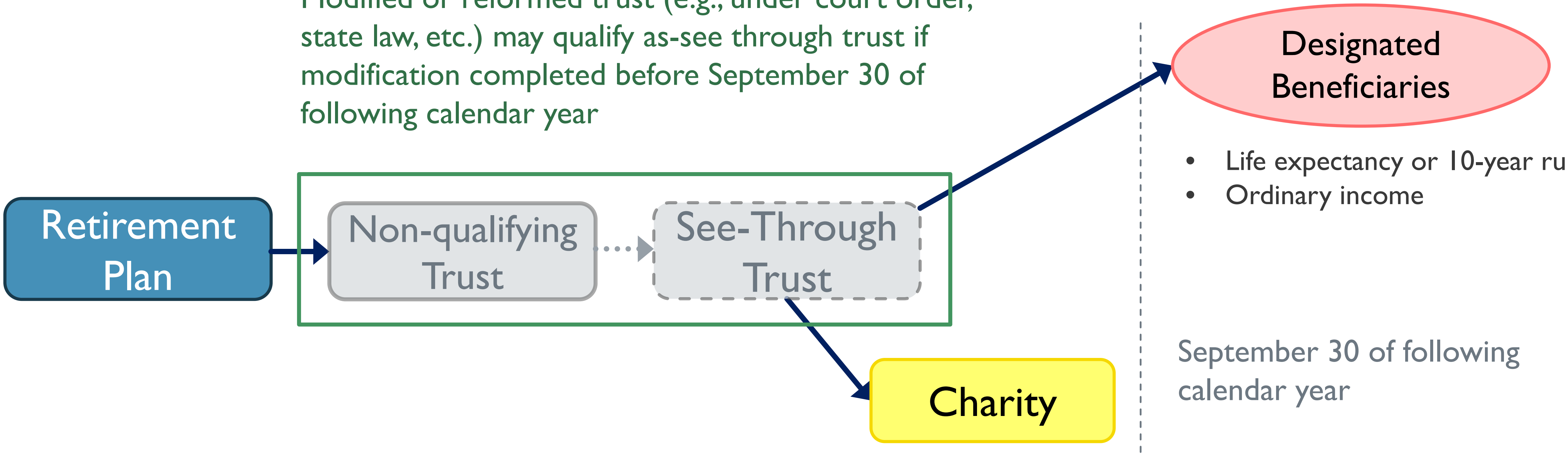


4. TRUST OR ESTATE DISPOSITION TO CHARITY

Modified or reformed trust (e.g., under court order, state law, etc.) may qualify as-see through trust if modification completed before September 30 of following calendar year



- Life expectancy or 10-year rule
- Ordinary income

September 30 of following calendar year

- Fractional share
- Tax-exempt

4. TRUST OR ESTATE DISPOSITION TO CHARITY

- **Income Tax Considerations**
  - Pecuniary gift (fixed dollar amount or defined formula) to charity may trigger capital gain to trust on IRA proceeds—while fractional share is tax-exempt (See Chief Counsel Advice (CCA) 200655020)
  - Charitable distributions from a trust normally do <u>not</u> qualify for a distributable net income (DNI) deduction (See IRC § 651, 661)—but an income tax deduction is available for trust distributions that qualify under IRC § 642(c)
  - Estates (or "qualified revocable trusts" that elect to be taxed as estates under IRC § 645) are allowed a deduction for set-aside of funds for charity to be paid in the future

5. CHARITABLE GIFT ANNUITY

- **What is it?**
  - In exchange for a contribution of cash or appreciated assets, a charity issues a contract for annual payments to a named individual (may or may not be donor)
  - Distributions must be made over actuarial life expectancy of beneficiary (<u>not</u> term of years)
  - Minimum payout of 5% required; current percentage is set by the American Council on Charitable Gift Annuities based on annuitant's life expectancy

5. CHARITABLE GIFT ANNUITY

- **Tax Consequences**
  - During life, an income tax charitable contribution deduction allowed for charitable remainder interest (amount of contribution LESS the present value of the annuity based on beneficiary's life expectancy and IRS actuarial tables
  - Testamentary distribution to CGA produces an estate tax charitable deduction equal to the charitable remainder interest
  - Annuity distributions to beneficiary are normally taxed as ordinary income

6. TESTAMENTARY CHARITABLE REMAINDER TRUST

- **Why?**
  - For the charitably inclined, Charitable Remainder Trusts (CRTs) offer an alternative "stretch-out" vehicle for non-eligible beneficiaries
  - Distribution to the CRT is tax-exempt and qualifies for *unlimited* **estate tax charitable deduction** equal to the present value of the remainder interest based on the IRC §7520 rate and designated life or term of years

6. TESTAMENTARY CHARITABLE REMAINDER TRUST

- **How?**
  - Annuity or unitrust CRT options (CRAT, CRUT, etc.)
  - Life expectancy or term of years (maximum 20 years)
  - Distributions from CRT taxed on a tiered (“worst first”) basis:
    - 1st ordinary income, 2nd ST capital gains, 3rd LT capital gains, 4th Other Income, 5th Return of Basis

6. TESTAMENTARY CHARITABLE REMAINDER TRUST

- Basic CRT Provisions
  - A donor transfers property, cash or other assets into an irrevocable trust (which receives a "carryover basis" in the assets, i.e., the same basis as it would be in the donor's hands)
  - The trust pays income to at least one living non-charitable beneficiary.
  - The payments continue for a specific term of up to twenty (20) years or the life of one or more non-charitable beneficiaries.
  - At the end of the payment term, the remainder of the trust passes to one) or more qualified U.S. charitable organizations.
  - The remainder donated to charity must be at least a calculated 10% present value of the initial net fair market value of all property placed in the trust.

6. TESTAMENTARY CHARITABLE REMAINDER TRUST

- Types of CRTs
  - Charitable Remainder Annuity Trust (“CRAT”) 5% minimum payout
  - Charitable Remainder Unitrust (“CRUT”) 5% minimum payout
  - Net Income Charitable Remainder Unitrust (“NICRUT”) lesser of income or 5%
  - Net Income Make-up Charitable Remainder Unitrust (“NIMCRUT”) lesser of income or 5% with deficit make-up account
  - Combination NICRUT or NIMCRUT that “flips” to a CRUT after a designated event (“Flip-CRUT”)

6. TESTAMENTARY CHARITABLE REMAINDER TRUST

- Does a CRT make sense?
  - Charitable intent?
  - Does the 10-year rule apply? Could CRT terms substantially "stretch-out" taxable distributions?
  - Is the estate taxable? Are there sufficient non-IRA funds available to pay estate tax?

EXAMPLE OF 50 YEAR OLD INDIVIDUAL BENEFICIARY

Beneficiary Projections at Settlor's Death	**CRUT**		**10-Year Rule**
Non-charitable Beneficiary Life Expectancy	31.4		31.4
IRC §7520 Rate	5.60%		5.60%
Beginning Principal	$ 2,000,000		$ 2,000,000
	Minimum	**Maximum**	
Minimum and Maximum Payout	5.0000%	9.5879%	N/A
Projected Payout (Nominal Total)	3,749,407	3,684,520	3,320,725
Income Tax Liability (Single Taxpayer)	560,189	598,405	903,825
PV of Net After-Tax Distributions to Son	1,411,294	1,642,902	1,613,313
Charitable Estate Tax Deduction	517,520	200,000	-

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PV to Son *PLUS* Charitable Deduction	***1,928,814***	1,842,902	1,613,313

CRT can "stretch" more value out of IRA proceeds for beneficiaries!

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