



VIRGINIA ESTATE  
& TRUST LAW



# The Importance of Beneficiary Designations Under the Secure Act

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# ROADMAP →

- Secure Act
  - A New Perspective!
- Charitable Giving Opportunities
- Secure Act 2.0



# SECURE ACT RECAP

- Effective 1/1/2020
- RMD age extended to 72 (updated under Secure Act 2.0)
- Eliminates stretch IRA for most inherited accounts, requiring 10-year payout with no annual withdrawal requirement for most beneficiaries
- 10-year rule does not apply to: surviving spouses, minor children (but not grandchildren!), disabled or chronically ill beneficiaries; trusts f/b/o those individuals, and beneficiaries who inherited accounts from owners who died prior to 1/1/2020 (but 10-year rule applies when that beneficiary dies)
- No one-size fits all approach to new rules



# SECURE ACT – WHO IS THE BENEFICIARY?

- Individual
  - Spouse – life expectancy with option to rollover
  - Adult child – 10-year rule (RMDs at based on parent’s life expectancy if parent died on or after RBD starting in 2023)
  - Minor child – life expectancy until 18, then 10-year rule
- Trust
  - F/B/O spouse, adult child, or minor child (a/k/a designated beneficiary trust) – same treatment as outright to individual
    - Beneficiary designation looks like “John Smith Trust FBO Jane Smith”
  - Non-designated beneficiary trust – 5-year rule
    - Beneficiary designation looks like “John Smith Trust”
- Estate – 5-year rule



# SECURE ACT RMD CHART

	Outright	Conduit Trust	Designated Bene. Trust (“See Through Trust”)	Non-Designated Bene. Trust
Non-Eligible Beneficiary	10 Year Rule	10 Year Rule	10 Year Rule	<i>Before RBD:</i> 5 Year Rule  <i>After RMD:</i> Ghost Rule
Surviving Spouse	Life Expectancy (option to rollover)	Life Expectancy	10 Year Rule	
Minor Child	Life Expectancy Until Majority	Life Expectancy Until Majority	10 Year Rule	
Beneficiary <10 Yrs. Younger	Life Expectancy	Life Expectancy	10 Year Rule	
Disabled/ Chronically Ill	Life Expectancy	Life Expectancy	Life Expectancy	



# SECURE ACT – PROPOSED REGULATIONS

- Proposed to become effective on January 1, 2022; however, Notice 2022-53 from the IRS said they would not be effective before January 1, 2023
- “At Least as Rapidly” Rule
  - Beneficiaries who are subject to the 10-year rule must also take annual distributions based on their life expectancy
  - This rule does not apply when the participant dies before the RBD
- Defines unclear terms in SECURE Act
  - Age of majority = 21
  - Disabled beneficiary = if by the participant’s death, Social Security has determined that the beneficiary is disabled



# SECURE ACT – PROPOSED REGULATIONS

- See-Through Trusts
  - Allows underlying beneficiaries to be treated as designated beneficiaries
  - (1) Trust is valid under state law; (2) trust is irrevocable or becomes irrevocable at the participant's death; (3) trust must contain identifiable beneficiaries; and (4) trust document provided to account administrator by certain deadlines after date of death
- Important Questions
  - What annual distributions are required after the participant's death, if any?
  - Is there an “outer limit year” in which the account must be depleted?





## Secure Act – A New Perspective!

- Living off large distributions from an inherited retirement account enables the beneficiary to afford to increase new salary deferrals into employer retirement plans and/or make new contributions to traditional or Roth IRAs
- Example: Grandpa dies at age 70 and left \$100,000 in his Roth IRA to his adult son, age 45.
  - Traditional planning: Delay all distributions until late in the 10<sup>th</sup> year, then take all money tax-free. If the \$100,000 grew at 7%, the son would get around \$200,000 at age 55. What would the son do with the \$200,000 of tax-free income?
  - New perspective planning: Son works for an employer with a Roth 401(k) and is currently making contributions of \$2,500/year. Son could withdraw \$20,000 from the inherited for the year of death and live on that amount while deferring \$20,000 of new contributions into his employer's Roth 401(k). If his income allowed, he could also withdraw another \$6,500 from the inherited IRA and contribute it to his own Roth IRA. If married and if income allowed, they could do the same for the son's wife. Moving \$53,000 from Grandpa's Roth IRA in the first year.



# Secure Act – A New Perspective!

- Why follow the new perspective plan?
  - After draining inherited IRA, son stops facing any further RMDs (potentially 3 sets of RMDs if Grandpa died after RBD)
  - Son places himself in an almost identical position as a surviving spouse eligible designated beneficiary
  - Money can grow tax-free for retirement
- What if Grandpa's \$100,000 had been in a traditional IRA?
  - Son could take a \$20,000 withdrawal from the inherited IRA. He could live on the withdrawn money and be able to afford to salary defer a new \$20,000 into his 401(k) at work. If the son made \$100,000/year, his income tax return would show W-2 income of \$80,000 and a taxable IRA distribution of \$20,000. No change in taxable income.
- What if Grandpa's IRA had been larger?
  - The concept just takes longer. Son and wife could move at least \$750,000 over 10 years by contributing maximum amounts to 401(k)s and IRAs.



# SECURE ACT 2.0

- Passed December 29, 2022; Builds on 2019 SECURE Act
- RMD Changes:
  - Individuals turning 72 during 2023 or later will start their RMD at age 73
  - Individuals turning 74 after December 31, 2032, will start their RMD at age 75
  - Starting in 2023, the penalty for failing to take an RMD will decrease to 25% of the RMD amount not taken (currently 50%). The penalty will be reduced to 10% for IRA owners if the account owner withdraws the RMD amount previously not taken and submits a corrected tax return in a timely manner.
- Roth Changes (a/k/a “Rothification” of Employer Sponsored Plans)
  - Workers age 50-plus earning \$145,000 or more are required to make catch-up contributions to a Roth account
  - Permits employers to offer employees the opportunity to characterize fully vested employer matching and nonelective contributions as Roth contributions
  - Eliminates pre-death RMDs for Roth accounts starting in 2024
  - SEP and SIMPLE IRAs can offer Roth options



## Secure Act 2.0

- **Qualified Charitable Distributions:**
  - Beginning in 2023, people age 70½ and older may elect as part of the QCD limit a one-time gift up to \$50,000 to a charitable remainder unitrust, a charitable remainder annuity trust, or a charitable remainder gift annuity
  - This amount counts toward the annual RMD if made directly from the IRA by the end of the calendar year



# Charitable Giving Opportunities

- Secure Act:
  - If beneficiary over 70.5 is still contributing to IRA, contributions reduce \$100K ceiling for qualified charitable distributions (QCDs)
  - DAFs do not qualify for QCDs
  - Consider funding/gift formulas in certain cases.
    - For example, “ I give the lesser of \$\_\_\_\_\_ or \_\_\_% of the Trust Fund assets to [charity name], reduced by any amount received by [charity name] at my death due to transfer by operation of law or beneficiary designation. My Trustee may rely on a statement from my financial advisor or other copy of a statement or beneficiary designation form when determining the amount of the gift or reduction in gift.”
    - Consider making the charitable donation in the beneficiary designation of the retirement asset in lieu of the will or trust, even if partial gift. More dollars will be left for individuals if you can pay less tax.



## Charitable Giving Opportunities

	No Designated Beneficiaries	Individual Designated Beneficiaries	Individual (70%) & Charitable (30%) Designated Beneficiaries
401(k) Value	\$1,000,000	\$1,000,000	\$1,000,000
Pay-out Period	5-year rule	10-year rule	10-year rule
Estate receives?	Estate pays \$390,000 in tax and receives \$610,000	N/A	N/A
Children receive?	Each child receives \$305,000	Each child receives about \$360,000 after 28% tax over 10 years	Each child receives about \$252,000 after 28% tax over 10 years
Charities receive?	0	0	Charity receives \$300,000
Total Tax	\$390,000	\$280,000	\$196,000



# Questions?

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