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RE: 2020 Guidance from Treasury Regarding Section 401 of the SECURE Act

Dear Ms. Weiser, Ms. Judson, and Mr. Tackney:

We are writing to request an overhaul of the existing interpretation of the required minimum distribution ("RMD") rules under IRC Section 401(a)(9) as they relate to trusts as beneficiaries of retirement plans after the death of an employee or owner ("participant"). These rules have been changed rather significantly by Section 401 of the Setting Every Community Up for Retirement Enhancement Act of 2019, Pub. L. 116-94, which was included in the Further Consolidated Appropriations Act, 2020 ("SECURE Act").

We are long-time Georgia tax attorneys specializing in trusts and estates law, and we have significant experience in dealing with the RMD rules. In fact, Richard recalls giving a speech to professional advisors on this topic in or about 1991. He also remembers purchasing the first edition of the T&E attorney's bible on this topic, "Life and Death Planning for Retirement Benefits," written by Natalie B. Choate. The RMD rules have come a long way since those fairly early days where the failure to make a timely irrevocable election by age 70 ½ had the effect of potentially locking in a horrific RMD election which could cause a one-year full payout after the retirement account owner's death. However, while the RMD rules have been fixed to work quite well when the beneficiary is an individual, the rules are still far from ideal when the beneficiary is a trust. Our comments relate to the RMD rules in effect when the beneficiary is a trust.

Richard is a member of the American College of Trust and Estate Counsel ("ACTEC"), and we realize that a brilliant group of ACTEC attorneys are already working very hard on providing comments to assist you in making the RMD rules, as they are currently structured, work properly in light of the changes made by the SECURE Act. Richard has already read a still preliminary draft of these comments, and he believes that they are clearly exceptional. However, we are writing to challenge your working group to go deeper with regard to the RMD rules as they apply to trusts as beneficiaries. And, before we get to our comments / challenge, we want to be clear that we are writing only as very concerned long-time T&E attorneys and not on behalf of ACTEC or any other organization.

A. Issue of concern.

At its core, the issue of concern is that the RMD's designated beneficiary ("DB") rules are way too restrictive when a trust that can accumulate retirement plan distributions is named as the retirement plan beneficiary, and thereby have the effect of forcing individuals to change the substance of their estate plans (i.e., how they wish to provide for their loved ones after their demise) in order to comply with the RMD's DB rules. I believe that these RMD restrictions do not reflect the reality of modern estate planning, especially after the SECURE Act.

In this regard, it is key to understand modern estate planning. We have discovered over the past decades that planning with various types of trusts can be extremely beneficial for our clients' families, especially from a state law, property rights perspective. Trusts provide significant control and asset protection benefits. In addition, we also learned from the U.S. Supreme Court in Clark v. Rameker, 134 S. Ct. 2242 (2014), that inherited IRA accounts are not protected in federal bankruptcy. After this case, protection of inherited IRAs from the claims of a beneficiary's creditors depends on applicable state law. Since you can never know for sure where family members may end up living, passing IRA accounts to an individual beneficiary means that the inherited IRA account may not end up being protected from the beneficiary's state law based creditor claims, just as these accounts are not protected under federal bankruptcy law. As a result, the beneficiary of a retirement plan account is often best designated as a trust for the child's (or other non-spouse loved one's) benefit, rather than designating the individual outright, even with mature, fiscally responsible individuals.

In most cases, naming a trust as the beneficiary of a retirement plan account is not being done for a tax advantage, but rather to take advantage of the state law benefits of trusts. When passing retirement accounts in trust to achieve state law benefits, the goal is normally to simply avoid losing income tax deferral flexibility otherwise available to an individual beneficiary under the RMD rules. As discussed below, it can often be difficult to use trusts to best take care of loved ones while also being able to take advantage of the same RMD rules that apply to individual beneficiaries of retirement accounts. We believe this issue can be resolved.

B. The three (3) trust options under the RMD rules and why each is a problem.

While we are well aware that you do not need an education on the RMD rules, we would like to provide some insight as to how we, as long-time T&E attorneys, see these rules. For purposes of brevity, we are not setting out all applicable requirements, but we have tried to go right to the most important requirements and concerns.

1. Conduit Trusts [Treas. Reg. Section 1.401(a)(9)-5, A-7(c)(3), Example 2].

The IRS will look through the trust to the life of an individual trust beneficiary ("conduit beneficiary") if the trust terms require that all retirement plan distributions to the trust must be immediately paid out to the conduit beneficiary. In this situation, all other possible trust beneficiaries are ignored for purposes of the RMD rules as they are considered to be "mere potential successor beneficiaries."

Before the SECURE Act, the conduit trust option was the standard in our practice, and we believe that this was also the majority view of most other T&E attorneys that were brave enough to recommend naming trust(s) as beneficiaries of retirement plan accounts after the participant's death. The only time we did not recommend the conduit trust option was when it would be highly imprudent to force any amounts to the conduit beneficiary, for example, where the primary beneficiary had special needs, was a serious spendthrift, or had dependency issues. Our reasoning for the conduit trust option being the standard before the SECURE Act was that RMDs based on the conduit beneficiary's life expectancy meant that the forced distributions would likely not be too significant, this was the simplest option for clients to administer, and the other two trust options were often poor choices, as will be discussed below.

However, after the SECURE Act, the conduit trust option is no longer the standard, it is just one of three often imperfect options. Because the Secure Act reduced the applicable distribution period ("ADP") for designated beneficiaries ("DBs") under the RMD rules from the beneficiary's life expectancy ("LE") to a 10-year cliff period, the use of a conduit trust now means that the entire retirement plan account balance would effectively need to be distributed outright to the conduit beneficiary by the end of the 10th anniversary year after the participant's death. From a planning perspective, the client must choose between full forced distribution (and the resulting loss of the trust's state law benefits) within an approximate 10-year period or among the two (2) other imperfect options.

The ADP based on the beneficiary's LE would still apply (at least to some extent) to Eligible Designated Beneficiaries ("EDBs"), and therefore conduit trusts may still make sense where intend to benefit certain types of EDBs (including the participant's spouse, someone not more than ten (10) years younger than the participant, and possibly, the participant's minor children) or where the 10-year distribution period is determined to be sufficient.

2. See-through accumulation trusts [Treas. Reg. Section 1.401(a)(9)-5, A-4, A-5, and A-6].

The good news is that see-through accumulation trusts permit retirement plan distributions to be accumulated (not forced out as with conduit trusts) and they qualify as DBs. In theory, this should be the preferred type of trust for non-spouse beneficiaries in most cases if the requirements are not onerous. However, the reality is that the requirements are fairly onerous. To qualify, two significant requirements must be satisfied. First, the possible beneficiary with the shortest LE (that is not considered to be a mere potential successor beneficiary) must be identifiable on the participant's date of death, and second, all such countable beneficiaries must necessarily be individuals.

To understand why these requirements are so significant, you need to understand that (i) benefitting charity and paying estate and trust expenses are not evil uses of retirement plan funds that should prevent access to the normal RMD rules for DBs (ii) T&E attorneys have a strong desire to create flexible trusts that will self-adjust with changed circumstances and enable modifications and tax planning via limited and general powers of appointment, (iii) potential trust beneficiaries will <u>always</u> include non-individuals, and (iv) even if you could argue that the current Identifiable rules as to accumulation trusts were reasonable before the SECURE Act, they surely are not reasonable after the SECURE Act.

We need to emphasize the troubling nature of the mere potential successor beneficiary rule as applied to accumulation trusts. First, trusts will always have another possible beneficiary, up to and including escheating to the state, which is clearly a non-individual. As far as we can tell, the IRS has taken the position in numerous Private Letter Rulings ("PLRs"), that a simple example in the Treasury Regulations with limited stated facts created a hard and fast rule which seems to ignore basic trust law. See Example 1 of Treas. Reg. Section 1.401(a)(9)-5, A-7(c)(3). Forgive us if we are misstating it here, but this is our understanding. If upon the death of a previous beneficiary, the next beneficiary gets all of the retirement funds outright without any contingencies or conditions whatsoever, then all beneficiaries thereafter can be ignored as mere potential successor beneficiaries.

Again, please forgive us if we are missing something, but we have found this example and the hard and fast rule that has somehow come from it to be totally arbitrary. You just need to go to the wording of Example 1 that states, "A's children, who are all younger than B, are the sole remainder beneficiaries of Trust P. No other person has a beneficial interest in Trust P." Trust law simply does not work this way. A risk always exists that an individual may die before receiving their full benefits under the terms of a trust. If a beneficiary dies, the trust agreement or applicable state trust law will always find a successor beneficiary of some type, contingent or not. Let me repeat this for emphasis, always! Because the Treasury Regulations ignore basic trust law, they cause confusion. To date, we are not aware of any legally citable authority that fleshes out this issue.

So, what is the problem with using see-through accumulation trusts? The various restrictions end up causing significant limitations on a client's substantive estate plan. When we draft these types of trusts, we are essentially forced to create separate trust shares to hold only the retirement plan accounts / benefits to limit the various restrictions to the extent possible. Of course, this causes otherwise unnecessary extra administrative costs and hassle, and potentially significant limitations on a client's testamentary intent at least as to the retirement plan accounts.

3. Non-DB Trusts.

Since non-DB trusts permit retirement plan funds to be accumulated and these trusts are not subject to any limitations, they would be the best type of trust to hold retirement plan accounts if it were not for their negatives. These negatives include: (i) the difference in the ADP, which generally changes to either the 5-year cliff rule (if the participant dies before the Required Beginning Date ("RBD") or the ghost LE (if the participant died on or after the RBD); (ii) the RBD for Roth IRAs being limited to the 5-year cliff rule; and (iii) the very poor outcome for qualified retirement plan accounts (i.e., they cannot be rolled over to an inherited IRA and therefore the distribution options are limited by the retirement plan's terms, which normally require full distribution within a short 1 year or so period).

C. Requested modifications to the RMD's DB rules as to trusts.

We believe the following modifications to the RMD rules will provide a significant benefit to both taxpayers (who will no longer have to modify their substantive estate plans to satisfy multiple technical requirements under the RMD rules nor suffer negative tax consequences from failing to do so) and the IRS (who will have resources freed up by no longer being asked to reply to a significant number of PLR requests nor have to expend limited resources on ensuring compliance with these various technical requirements).

1. Streamline and simplify the RMD rules as to trust beneficiaries.

   a. Trusts where the only current beneficiaries include an EDB and his or her descendants, as broadly defined.

Any trust in which either (i) an eligible designated beneficiary ("EDB") is the sole current beneficiary or (ii) an EDB and his or her descendants (broadly defined) are the only current beneficiaries shall have an ADP based on the EDB's LE (subject to changing to the 10-year cliff rule where the EDB is the participant's minor child and the child has attained age 26, the max age to attain the age of majority under the SECURE Act). If the trust has more than one EDB as a current beneficiary, then the ADP will be based on the LE of the EDB with the shortest LE. If the EDB's LE is less than 10 years, then the standard 10-year cliff rule will apply.

b. All other trusts.

All other trusts will be subject to the general 10-year cliff rule.

c. Definition of a current beneficiary.

A current beneficiary is entitled or eligible to receive current distributions from the trust that could be satisfied with an interest in a retirement plan.

2. Requested modification to the separate share rules and enable changes after the participant's death.

Current RMD rules result in different ADP outcomes depending on the beneficiary designation naming an estate or a trust which later splits up into separate trust shares vs naming the ultimate separate trust shares directly. If the initial beneficiary is an estate or other non-DB, then outside PLR approved exceptions, the result is a non-DB beneficiary status regardless of who actually ends up receiving the retirement plan account funds. If the initial beneficiary is a trust with multiple beneficiaries that will end up being split into shares for the primary benefit of each separate beneficiary, then outside PLR approved exceptions, the ADP is based on the individual with the shortest LE in the initial trust, or the ADP is based on having a non-DB beneficiary if the initial trust includes any countable non-individual beneficiaries.

My question is why? If the goal is to cause significant technical obstacles to reduce potential abuse, then mission accomplished. However, especially after the SECURE Act, such technical traps should no longer be needed. Why not simply give the parties until the beneficiary determination or finalization date (September 30th of the year after the participant's death) to fix any problems with the beneficiary designation after the participant's death? We believe the RMD rules should not be applied until the beneficiary determination or finalization date. For example, let's say that the beneficiary designated for a retirement plan account was the participant's estate (to be controlled by their Will) or their Revocable Living Trust ("RLT"), the parties would have until September 30th of the year after the participant's death to distribute the retirement plan account to wherever it is destined to end up under the Will or RLT. While current law permits very limited fixes during this time period, I see no reason not to fully expand this flexibility in a taxpayer friendly manner.

Because of the reduction in potential income tax deferral resulting from the SECURE Act, I hope that you will see that this is the perfect time to take an ax to these rules rather than the normal scalpel. You may be thinking that the Treas. Dept and IRS do not make such radical changes to such long-standing tax rules. However, precedent exists for doing just that. See the check-the-box Regulations under IRC Section 7701 that became effective on January 1, 1997. These Regulations radically changed the process for determining how an entity would be classified for tax purposes. Prior to the Regulations, the facts and circumstances tests caused significant resources being spent on this issue by both the IRS and taxpayers. These Regulations effectively ended this entire complex ordeal. It was a brilliant move, and this same global simplification ideal now needs to be applied to the RMD rules.

We understand that these recommended changes will take more in-depth thought to make sure all necessary provisions are properly modified, but we have a high level of confidence that we will be able to get the assistance of ACTEC members or other very qualified attorneys to aid in this project.

Please feel free to contact us if you would like to discuss these proposed modifications further. Thank you for your consideration.

Respectfully submitted,

Richard M. Morgan

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