<u>Recapturing the “Stretch” in your IRA</u>

Last December, the bipartisan *SECURE ACT* was passed into law. Politicians and investors seem generally pleased with the new options available to retirement fund owners, such as the ability to contribute into the retirement years, as well as the ability to annuitize an income stream.

Of course, there are always two sides to the coin, for <u>when Uncle Sam giveth</u>, <u>he also taketh away</u>.

Most married people designate their surviving spouse as the beneficiary of their qualified retirement plan. The survivor usually rolls the plan over into his or her IRA. When either a single person or surviving spouse has deceased, the beneficiary designation will ultimately go to the original owner’s named beneficiaries. If favorite charities are beneficiaries, the fund is distributed to them entirely tax-free, usually making it the first asset a well-tuned estate plan gives to charity. As for leaving the monies to heirs, the new law mandates in most cases, that all funds must be distributed within ten years if the recipient(s) is ten or more year’s younger than the fund owner.

Prior to this year, an IRA beneficiary was able to “stretch” the IRA payout over their life expectancy. Assume Ted owned a traditional IRA worth $2,000,000 and passed away in 2019, designating his daughter Carole (age 30) as the beneficiary. Carole’s job pays her roughly $42,000 per year. Instead of cashing in the IRA and recognizing the full $2,000,000 as immediate taxable income, Carole chose to “stretch” the payouts over her life expectancy, starting at about $37,000 the first year. By opting for the “stretch” Carole reduced her income tax and benefitted from tax-free growth for many years.

Now let’s pretend Ted passes away in 2020. Assuming she doesn't take the IRA in one lump sum (a worst case scenario, but all too common with heirs), Carole’s likely smartest available option is to receive the $200,000 per year over the ten years following her father’s death, catapulting her from the modest 22% federal income-tax bracket to the 35% bracket. If the Trump Administration’s tax cuts expire in 2025, her tax liability might even be a whole lot higher. As you can see, Uncle Sam will be smiling when she pays significantly more in taxes each year, mostly with her dad’s money!

Except in extreme health or medical situations, there are no more stretch provisions nor conduit trusts allowed for heirs, as so many have planned in their will to force the recipient to do the responsible thing and pace the inheritance. ~~-~~As a result, the CBO predicts that $15.7 billion in new tax revenue will supply federal coffers.

There are ways to avoid that unintended consequence on your heirs.

As mentioned earlier, one way is to gift these funds to a charity after the owner dies, causing no recognition of income taxes, besides also creating a dollar-for-dollar estate tax deduction. A second option would appeal to the fund owner who wishes to leave every penny they can to their heirs and who would rather also help others through worthy charities instead of the government. Utilizing a “Give-it-Twice" (G-2) charitable vehicle can be a wonderful way to effectively recapture the old "stretch” for your heirs while eventually creating a dynamic, and yes exciting, philanthropic footprint.

One G-2 option involves the classic Charitable Remainder Trust (CRT). Using the above example, if Ted's attorney installs a CRT in Ted’s estate plan (which is revocable until death), the CRT would receive his IRA and liquidate it entirely tax-free, satisfying the new IRS requirement. The year following his death (or his spouse's death), the CRT begins making a 5% annual payment to his daughter, either for her lifetime or for a term of up to 20 years.

If the latter course is chosen and the market behaves itself, Carole should receive the entire $2,000,000+ over said 20 years (five times twenty equals 100%) before the CRT is liquidated, distributing the "remainder" to Ted's favorite qualified charities. Put another way, his daughter receives 100% of the IRA and his favorite charities receive 100%, thus giving it twice. Talk about an amazing legacy!

Or Ted could just keep his estate plan as is and let his daughter make a hefty 35% contribution to Uncle Sam with Ted’s money.

Marc Littlecott, CAP® is Director of Gift Planning at the SDSU Foundation. His team assists people wishing to benefit charitable causes to investigate planned giving options, developing charitable solutions they can take to their qualified advisors for consideration and implementation. Call the SDSU Foundation to learn more at 605-697-74~~5~~75 or visit www.sdstatelegacy.org