

How a Trusteed IRA Can Improve Your Retirement Plan

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If your goal is to ensure that your retirement plan is available to provide income, tax-deferred growth, and long-term security for your family, then you should consider the benefits of a Trusteed IRA. Most people name their spouse as the primary beneficiary and their children as the secondary beneficiaries of their retirement plan. This typical beneficiary designation results in three potential risks: (1) your spouse may leave your retirement plan to his or her new spouse after you die, (2) your children may ignore the deferral option, cash out the retirement plan as soon as they inherit it, and blow through the money like a tornado in a trailer park, or (3) your IRA may be lost to creditors if your children get into financial problems of their own. A Trusteed IRA is an easy, simple, and inexpensive way to avoid all of these risks.

What is a Trusteed IRA?

A Trusteed IRA is typically provided by a financial institution, and it has the same tax rules and benefits of a traditional IRA.

With a traditional IRA, your named beneficiary assumes full control of the account after you die. This means that the beneficiary can drain the account as fast as he or she wants and can change the beneficiaries as he or she wishes. A Trusteed IRA allows you to control the timing and amount of future distributions and the class of potential future beneficiaries.

For example, your Trusteed IRA could be designed as follows: (1) during your life, the trustee will pay you the required minimum distributions and as much of the principal as you request; (2) during your spouse's life, the trustee will pay your spouse the required minimum distributions and as much of the principal as your spouse needs (after other resources are utilized) to maintain his or her health, support, and maintenance in accordance with the accustomed manner of living (without the option for your spouse to name someone other than your children as the beneficiary); (3) after the death of your spouse, the IRA will be divided into separate IRA accounts for your children; (4) your children will then receive



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the required minimum distributions based on their own life expectancies. Other available options to you in a Trusteed IRA are to give your children access to the principal at such times and in such amounts as you designate (and this could be different for each child), and you could choose to limit the potential beneficiaries to whom your children can give the IRA after their death.

Why Don't I Name My Family Trust as the Beneficiary?

If you name your family trust as the beneficiary of your IRA, chances are that the trust will not qualify for the favorable minimum distribution rules that apply to individual beneficiaries. This means that your heirs may be required to take the money out of the IRA within a short time period, resulting in much higher income taxes and no more opportunity for long-term tax deferral. Therefore, it is not wise to include a family trust as the beneficiary of a retirement plan. You could hire an attorney to create a conduit trust or accumulation trust, which would provide similar benefits to a Trusteed IRA, but this

will be more expensive and complicated than a Trusteed IRA.

Why Don't I Name My Children Individually as Beneficiaries?

Studies show that most inheritances are completely spent within seventeen months.¹ Most inherited IRAs are cashed out immediately despite the option for the heirs to defer distributions over their life expectancy. By naming individual beneficiaries, you risk the possibility that your heirs will spend the money immediately instead of taking advantage of the opportunity it gives them for tax-free growth and greater retirement security.

Another disadvantage of naming individual beneficiaries is that the inherited IRA could be lost to their creditors. The United States Supreme Court recently ruled that an inherited IRA is not eligible for the same protection from creditors as an IRA that is owned by the person who has funded the IRA.² The best solution to avoid these disadvantages is a Trusteed IRA.

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Other Benefits of a Trusteed IRA

In addition to the benefits listed above, a Trusteed IRA can also provide the following benefits: (1) a Trusteed IRA is very simple and inexpensive to establish; (2) it is easy to convert a traditional IRA to a Trusteed IRA; (3) a Trusteed IRA provides continuity of management and integrity of purpose over many years or multiple generations; (4) a Trusteed IRA is especially applicable to a second-marriage situation where each spouse wants to be sure the original plan is not altered by a surviving spouse; (5) a Trusteed IRA is very well protected from creditors, bankruptcies, and divorces; (6) a Trusteed IRA allows you to give a spouse or other beneficiaries a limited power to make changes within the scope that you allow (such as a power to change future beneficiaries among your descendants but not allowing changes outside of the family); and (7) it is easy to make amendments or restatements to a Trusteed IRA during your lifetime.

How a Trusteed IRA Would Work

Craig worked and scrimped and saved for many years to build up a substantial 401(k) retirement plan. Craig loved his wife and children, but he knew that they were not good about saving, investing, or managing money. One of his children had a rocky marriage, one had financial problems, and one had a spouse that was likely to spend anything the child ever received. Craig sought advice about how to preserve his assets for the long-term security of his family. Craig's financial advisor told him about a Trusteed IRA. Craig and his wife elected to roll his 401(k) into a Trusteed IRA that would pay the required minimum distributions to them for life, and then to their children for life, with no one having power to change the beneficiaries. Each of their children would then have the power to set the terms for the next generation. Craig was glad to know he could change this at any time, but for the time being, it gave him great peace of mind. He was also happy to find that the Trusteed IRA was inexpensive, and the entire set-up process took less than an hour.

Craig died unexpectedly at the age of seventy. His wife remarried, and her new husband moved into her home so he could sell his home and invest all he had in his dream business. The dream

business turned into a nightmare that drained the remainder of the couple's savings. Craig's wife tried to take the principal from the Trusteed IRA to help with the dream business, but the Trusteed IRA prohibited distributions of principal for such a purpose. Her new husband went bankrupt, but she still had the Trusteed IRA to provide income to her for life.

Craig's wife did not want to leave her new husband destitute so she added his name as a joint tenant on the family home. She attempted to name him as a beneficiary on the Trusteed IRA; however, the Trusteed IRA did not allow her to change the beneficiary. When she died, the new husband got the home and left it to his children from a prior marriage.

After the death of Craig's wife, Craig's children and their spouses were furious that they could not liquidate their share of the Trusteed IRA. Even though they were angry at first, they did enjoy the

monthly income it gave them for the next thirty years. They appreciated this even more when they realized that this was the only asset that survived all those years and that most of their other assets had been spent or lost to divorce or other financial problems. They also marveled at the tax-free compounded

growth that had occurred over the many years since Craig had died. After witnessing the blessing this Trusteed IRA had been in their own lives, Craig's children chose to leave it for their own children under similar terms and conditions.

Conclusion

If your goal is to ensure your retirement plan is able to provide income, tax-deferred growth, and long term security for your family, a Trusteed IRA may be a good option for you. It may give you peace of mind, knowing that your hard earned money will not be blown or diverted to spouses, creditors, or anyone else outside of your family.

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1. Texas A&M Foundation, *Secure Your Heirs' Inheritance with Thoughtful Estate Planning*, (July 8, 2015).
2. *Clark v. Rameker*, 134 S. Ct. 2242 (2014).