Benefits of Naming a Qualified Individual Conduit Trust or a See Through Accumulation Trust as the Beneficiary of Your Individual Retirement Accounts, Pensions, Profit Sharing Plans and Other Retirement Plans

WHAT IS A QUALIFIED INDIVIDUAL CONDUIT TRUST?

A Qualified Individual Conduit (QIC) Trust is a specially designed trust that satisfies the guidelines set forth by the Internal Revenue Service for naming a trust as the beneficiary of a qualified retirement account in place of naming an adult individual as the direct beneficiary. Special provisions apply when a beneficiary is a minor child, a spouse, a disabled or chronically ill person or is less than ten years older than the participant. The first question that comes to mind is why bother with a trust, just name the child directly as the beneficiary. The following table summarizes the primary differences:

		Differences	
		Treatment if outright to Beneficiary	Treatment in QIC Trust for Beneficiary
1.	Adult Beneficiary may stretch the payments over ten years	yes[1]	yes
2.	Money available if beneficiary has real needs	yes	yes
3.	Beneficiary may cash IRA in and spend all the money unwisely	yes	no
4.	Spouse can get assets in a divorce	yes	no[2]
5.	Creditors of beneficiary can attach	yes	no[3]
6.	Beneficiary may control investments of IRA	yes	yes
7.	Beneficiary can waste principal, give it away	yes	no[4]

Notes

Note 1 Only if beneficiary chooses to stretch. A beneficiary may withdraw all or most of the IRA immediately and spend the money. With a QIC Trust the special trustee will confer with the beneficiary to distribute the funds to the best tax advantage of the beneficiary.

Note 2 Limited access to principal but spouse can attach once distributed to beneficiary.

Note 3 Limited access to principal but creditors can attach once distributed to beneficiary.

Note 4 You can limit the persons to whom the beneficiary leaves any IRA balance at the death of the beneficiary.

A QIC Trust will assure you that your adult beneficiaries will not just take the money out of your retirement account and spend it unwisely, finding themselves with a big income tax bill the next April 15th. Also, with a QIC Trust your hard earned retirement assets will not be subject to a predator in a frivolous lawsuit brought against your beneficiary. (This protection is **not** available if your beneficiary is directly named as a beneficiary.)

WHO CONTROLS THE QIC TRUST?

The QIC Trust has two trustees: the named successor trustee (most often this is the designated income beneficiary) who has almost all of the power over the trust, and the special trustee whose job is to authorize distributions from the plan over the required time to achieve the best tax advantage for the beneficiary.

<u>What authority does the Successor Trustee have</u>?

- Controls the assets in the plan
- May make all investment decisions in the plan
- May buy or sell plan assets
- May invest in any investments that you as owner of the plan may make

<u>What authority does the Special Trustee have</u>?

The special trustee will consult with your beneficiary to distribute funds to the maximum tax advantage of the beneficiary. You can give guidelines to the special trustee as to allocation of additional income or principal to the designated beneficiary during the required time period.

WHAT ARE THE BENEFITS OF A QIC TRUST FOR YOUR BENEFICIARIES?

1. Beneficiary of a QIC Trust for an IRA

The "ten year rule," or the ability to take distributions any time within the ten year period, is available regardless of whether the designated beneficiary is a person or a QIC Trust. However, when a person is named the designated beneficiary, that person does not have to follow your wishes and may decide a new sports car or trip around the world is a better use of their inheritance. With a QIC Trust, the terms of the trust utilize a special trustee to consult with your beneficiary to distribute funds to the maximum tax advantage of the beneficiary. This gives the special trustee the opportunity to meet with the beneficiary and explain the different options available and advantage of timing when to distribute funds.

In order to be sure that the QIC Trust is effective, it will be necessary for you to send a change of beneficiary form to the custodian or the plan administrator of each tax-favored retirement plan that you wish to be governed under the provisions of the QIC Trust.

As used in the QIC Trust, "tax-favored retirement plan" shall include a corporate or self-employed ("Keogh") pension, profit sharing and stock bonus plan that is "qualified" under Section 401(a), an individual retirement account (IRA) created under Section 408, a Roth IRA established under Section 408A, or a tax-sheltered annuity (or mutual fund) arrangement established under Section 403(b) and all such similar plans that may be available to persons presently or in the future. All of the aforesaid sections refer to sections of the Internal Revenue Code.

The QIC Trust can be designed to let the designated beneficiary or any other party named to manage the investments in the individual retirement account. This is a flexible option to give the beneficiary as much or as little control over the funds as you desire.

The major benefit of a QIC Trust is to provide a greater benefit to your heirs than they could obtain even with an outright cash bequest of a similar amount. This can be especially beneficial if the designated beneficiary is a very young person, such as a young child who will need expert guidance.

2. Provide Extra Retirement Income for Your Beneficiaries

Most clients feel their children or grandchildren are not saving for retirement and will later regret the lack of money in their retirement years. There is also a variation of the QIC Trust that allows accumulation of funds rather than requiring immediate payment to the beneficiary. With such a trust, referred to as a See Through Accumulation (STAT) Trust, you can be assured that the money will not be spent on frivolous items, but saved for the long term needs of your beneficiary. Rather than requiring that the distribution be paid directly to the designated beneficiary, a STAT Trust has provisions which allow all or a portion of the distribution to be retained in the trust for the future needs of the beneficiary. See below for more information on a STAT Trust.

3. **<u>Protection from Creditors or Spouse in a Divorce</u>**

A QIC Trust is designed to protect the principal of the trust fund from a spouse in the event of a divorce or from creditors if the beneficiary has creditor problems.

4. **<u>What Happens if Designated Beneficiary Dies Prematurely</u>**

If your designated beneficiary dies prematurely, the trust can limit the persons the beneficiary can name to receive the remainder of your property held in that IRA account.

SEE THROUGH ACCUMULATION (STAT) TRUST

A STAT Trust as mentioned above is used when you have substantial tax favored retirement accounts and one or more of your beneficiaries is faced with some issues as outlined in our Special Needs Trust section or if for any reason you desire that the distributions from the trust be limited in some manner.

A STAT Trust must meet all of the normal trust rules governing QIC Trusts plus several special IRS rules that permit you to use a person as the “designated beneficiary” for purposes of determining how many years the withdrawal of funds from the retirement accounts are to be determined, yet instead of distributing substantial funds annually to the beneficiary, the trustee may retain part or all of the funds in the trust and not distribute money to the beneficiary until sometime in the future pending a change in the status of the beneficiary. Thus this trust will combine many provisions from the normal QIC Trust with those of a Supplemental Needs Trust and/or Asset Protection Trust, plus certain special provisions and alternatives required by the IRS.

A STAT Trust is beneficial or necessary when the beneficiary has some type of issue, such as substance abuse, poor marriage, creditor issues, is unable to manage money, is prone to be taken advantage of by others, is a minor, has special needs, and other such issues which make it such that the beneficiary should not have access to large sums of money.

Since these trusts are unique to the individual needs of the beneficiary, supplemental planning is required for the client.

WHY NAMING YOUR REVOCABLE LIVING TRUST (RATHER THAN A QIC TRUST OR STAT TRUST) IS NOT THE BEST CHOICE

You may ask why not just name my Revocable Living Trust or a subtrust within my revocable living trust as a beneficiary? The primary reason is that the revocable living trust and subtrusts do not generally have the required IRS provisions to qualify as a conduit trust and generally will require that the plan proceeds be paid out immediately. Furthermore, in order to provide flexibility in the revocable living trust and its subtrusts, provisions are often made for multiple beneficiaries or rights in the trustee to withhold distributions under certain circumstances, accumulation of income and required distributions at certain ages, or many other provisions that may result in the trust having no "designated beneficiary" as defined by the IRS and, thus, such trusts will not qualify for a ten year payment schedule and may result in required distributions of retirement plan monies over a short period of time.

GENERAL RULES FOR NAMING BENEFICIARIES OF RETIREMENT PLANS

As a general rule, if you are married your spouse would be the primary beneficiary and the QIC Trust the contingent beneficiary. Then when the plan owner dies, the surviving spouse names the QIC Trust as the primary beneficiary. There are times when this rule may not apply, such as:

- Second marriage or blended families
- Spouse who may not be responsible
- Children with special issues

These and many more situations require a consultation with a professional to determine alternative courses of action.

SUMMARY

QIC Trusts or STAT Trusts are trusts specially designed to qualify under IRS Rules to permit the benefits to be paid over the permitted ten year payout program to minimize taxes. It also offers asset protection for the retirement account that is not available when an individual is named as the direct beneficiary. QIC Trusts and STAT Trusts offer many additional advantages as a method of leaving an individual retirement account balance to children, grandchildren, etc., and should be considered anytime a person has a substantial individual retirement account balance.

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IRS Circular 230 Disclosure

Pursuant to recently enacted U.S. Treasury Department Regulations and to ensure compliance with the requirements imposed upon us by the United States Internal Revenue Service, we are now required to advise you that, unless otherwise expressly indicated, any federal tax advice contained in this communication, including attachments and enclosures, is not intended or written to be used, and may not be used, for the purpose of (i) avoiding tax-related penalties under the Internal Revenue Code or (ii) promoting, marketing or recommending to another party any tax-related matters addressed herein.

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