

New IRA Opportunities in Estate Planning

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Estate planning options for clients with qualified retirement plans (e.g. 401(k), 403(a) or (b), 457(b) plans) have historically been limited. The Pension Protection Act of 2006 (the Act), which was signed into law on August 17, 2006, creates two new flexible options for individuals whose estates include qualified retirement plans: the Act allows non-spouse beneficiaries to rollover the inherited distribution into their own IRA and the Act provides for generous tax-free charitable contributions.

The Act provides an extremely favorable new provision for non-spouse beneficiaries of a qualified retirement plan. Non-spouse beneficiaries can elect to rollover inherited assets from a qualified retirement plan into an IRA established in their own name with minimum distributions based on the beneficiary's life expectancy. The non-spouse beneficiaries can continue to take advantage of income tax deferral in the account until the beginning date for required withdrawals (i.e. age 70 ½). The Act extends this favorable rollover treatment to trusts established for the benefit of non-spousal beneficiaries.

To qualify as a tax-free rollover, the funds must transfer directly from the original plan to the IRA (a trustee-to-trustee distribution) and the inherited IRA account must remain in the name of the original retirement account owner payable to the designated beneficiary.

The rollover does not generate any income taxes and the non-spouse beneficiaries will only be taxed when distributions are made from the IRA. Previously, rollover treatment was only available to a spouse and non-spouse beneficiaries were required to take distributions of the full amount of the retirement plan within five years or, in some cases, immediately following the person's death.

A separate provision of the Act allows certain IRA owners to make tax-free distributions out of IRA accounts directly to eligible charities. Prior to the Act, a taxpayer who wanted to make a charitable contribution from an IRA had to include the amount withdrawn in taxable income and then claim a charitable deduction. However, the charitable deduction is limited by the taxpayers adjusted gross income and does not always eliminate all the taxable income generated by the withdrawal.

For the 2006 and 2007 calendar years, individuals over the age of 70½ may transfer up to \$100,000 per year of their IRA benefits to public charities directly from their IRAs. These transfers will be credited against the minimum required distribution but will not be included in income. For individuals who satisfy all of the conditions, this new provision provides an excellent way to contribute retirement plan assets to charity without having to recognize any income while simultaneously removing those assets from the individual's estate and thereby reducing any future estate taxes.

With the passage of the Pension Protection Act of 2006, individuals whose estate plans include qualified retirement plans have much more flexibility in devising how to maximize the amount of wealth transferring to future generations.