



What You Should Know about Trusteed IRAs

The tax code allows IRAs to be created as trust accounts, custodial accounts, and annuity contracts. Regardless of the form, the federal tax rules are generally the same for all IRAs. But the structure of the IRA agreement can have a significant impact on how your IRA is administered. This article will focus on one type of trust account commonly called a "trusteed IRA," or "individual retirement trust."

Why might you need a trusteed IRA?

In a typical IRA, your beneficiary takes control of the IRA assets upon your death. There's nothing to stop your beneficiary from withdrawing all or part of the IRA funds at any time. This ability of your beneficiary to withdraw assets at will may be troublesome to you for several reasons. For example, you may simply be concerned that your beneficiary will squander the IRA funds.

Or it may be your wish that your IRA "stretch" after your death--that is, continue to accumulate on a tax-deferred (or in the case of Roth IRAs, potentially tax-free) basis--for as long as possible. Your intent to stretch out the IRA payments may be defeated if your beneficiary has total control over the IRA assets upon your death.

Even if your beneficiary doesn't deplete the IRA assets, in a typical IRA you normally have no say about where the funds go when your beneficiary dies. Your beneficiary, or the IRA agreement, usually specifies who gets the funds at that point. So, in a typical IRA, if you name your spouse as your primary beneficiary, your spouse could name children from a previous marriage, or a new spouse if he or she remarries, as the ultimate beneficiary of your IRA assets. A trusteed IRA allows you to control the ultimate beneficiaries of your IRA, by letting you specify contingent beneficiaries that cannot be changed by your primary beneficiary.

With a trusteed IRA, you cannot stop the payment of required minimum distributions (RMDs) to your beneficiary but you can restrict any additional payments. You can direct the trustee to pay only RMDs to your beneficiary. Or you can provide the trustee with discretionary authority to make payments to your beneficiary in addition to RMDs, e.g., for your beneficiary's health, welfare, or education. Or you can impose restrictions on distributions that last only until your beneficiary reaches a specified age. Trusteed IRAs can also be set up to qualify as marital, QTIP, and credit shelter (bypass) trusts, potentially simplifying your estate planning.

A trusteed IRA can also be a valuable tool during your lifetime. It can be structured so that if you become incapacitated, the trustee will step in and take over the investment of assets and distribution of benefits on your behalf, ensuring that your IRA won't be in limbo until a guardian is appointed.

Is a trusteed IRA right for you?

While trusteed IRAs can be as flexible as a particular trustee will allow (not all provide the same level of IRA planning services), they aren't right for everyone. In some cases, another approach might be more appropriate. For example, you may be able to assure that your IRA "stretches" after your death by instead naming a trust as the beneficiary of your IRA. If specific IRS rules are followed, RMDs can be calculated using your trust beneficiary's life expectancy (this is commonly called a "see-through" trust).

However, see-through trusts are generally more expensive, and more complicated, than trusteed IRAs. It's important that you consult an estate planning professional who can explain your options and make sure you choose the right vehicle for your particular situation.

OUTPERFORM.

Are My Trust, Fiduciary and Custody Assets Safe?

Over the years RFS has been asked many times to explain the safety of trust assets. The following is a good overview from the American Banker Association (ABA). If you have additional questions, please do not hesitate to contact us.

Understanding the difference between account types

Many bank customers are confused about the difference between deposit, trust, fiduciary and custodial accounts. Here are some simple answers.

Assets held in **deposit accounts** become liabilities of the bank. As such, deposits create a debtor-creditor relationship between the bank and the depositor. In exchange for the money deposited, a liability of the bank is created which is the bank's contracture promise to repay the amount on deposit plus, where applicable, interest. As a result of a recent change in the law, deposit accounts are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000 per individual per bank.

Assets, including certificates of deposit, held in **trust and fiduciary accounts** other than cash do not become assets or liabilities of the bank and are, indeed, segregated from the bank's assets. The bank acts as trustee or fiduciary to the account and, in this connection, provides investment management, investment advice and other services to the account. Account ownership remains vested in the individuals or entities for whose benefit the bank is acting as trustee or fiduciary and the assets are not subject to the claims of creditors. Cash in trust and fiduciary accounts that are transaction accounts that do not pay interest may be fully insured by the FDIC. Cash held in the trustee bank in other types of deposit accounts is insured up to \$250,000 and applicable law, such as C.F.R. Part 8, may require that any amount over \$250,000 must be fully collateralized by the trustee.

Assets, including certificates of deposit, held in **custodial accounts** in the trust department of a bank, other than cash, do not become assets or liabilities of the bank and are segregated from the bank's assets. The bank's role as custodian is to hold the assets for safekeeping, to collect dividends and interest and provide other similar services. Account ownership in the assets, other than cash, remains vested in the individuals or entities for whose benefit the bank is acting as custodian and the assets are not subject to the claims of creditors. Cash in custody accounts that is held in non-interest bearing transaction accounts may be

fully insured by the FDIC. Cash held in the trustee bank in other types of deposit accounts is insured up to \$250,000.

What happens if a bank fails?

Since **deposit accounts** become liabilities of the bank, it follows that the depositor would become a creditor in the event a bank failed. However, the FDIC generally fully insures depositors who funds are held in non-interest bearing transaction accounts. Other types of deposit accounts are insured for up to \$250,000 per individual per bank.

Since assets held in **trust, fiduciary and custodial accounts** (other than cash) do not become assets or liabilities of the bank (title is held by the account's owner(s), it follows that none of this property is subject to the claims of the bank's creditors. As a result, a failure of a bank will have no adverse effect on trust, fiduciary or custodial accounts: **they remain the property of the account's owner(s).**

In the event that a bank with trust, fiduciary or custodial powers fails, the FDIC will seek to transfer responsibility for administration of the accounts to a successor trust institution as quickly as possible. Provided this effort is successful, the account beneficiary would need to either accept this new arrangement or make provisions with the successor bank for alternative arrangements. Should the search for a successor trustee to the failed bank be unsuccessful, the FDIC will then promptly notify all affected beneficiaries to either personally reclaim their property or designate an alternate institution to which the trust, fiduciary or custodial property may be conveyed.

Therefore, the safety of trust, fiduciary and custodial assets is not dependent upon whether the bank has assets greater than its liabilities. Property held in these accounts belongs to the owner(s) of the accounts and would be unaffected by the bank failure.

