

See-Through Trusts - Identifying the Beneficiaries

Take-Away: Some trust beneficiaries of a *see-through accumulation trust* will now be ignored under the SECURE Act Final Regulations.

Aside: This topic arose in light of a telephone call and email exchange that I had with a Las Vegas attorney. He apparently had read one of my earlier missives on *see-through trusts* and he wanted to know if the recent Final Regulations altered my earlier observations on how an *accumulation see-through trust* was interpreted by the IRS. I advised that the Final Regulations made it easier to pass the *see-through rules for accumulation trust*. I was happy to confirm this understanding, but frankly I was more surprised that a lawyer in Nevada actually read what I wrote 9 months ago!

Background: I've covered the topic of *see-through trusts* before, but whenever there is 'good news' for lawyers it's nice to learn about it again. This is one of the changes in the required minimum distribution (RMD) rules caused by the SECURE Act. As was reported previously, the IRS issued Final Regulations with respect to the SECURE Act in late July, 2024. One of the helpful changes found in those Final Regulations deals with the *see-through trust* rules for accumulation trusts.

Designated Beneficiaries: By way of a short background, only *individuals* can be named as designated beneficiaries of a retirement account with the privilege of spreading those distributions from the inherited retirement account over an extended period. However, a trust is technically not an *individual*. If a non-individual is named as the beneficiary of a retirement account, the distributions from the account can only be spread over 5 years, not 10 under the SECURE Act, or over an eligible designated beneficiary's life expectancy.

See-Through Trust Rule: However, the earlier Regulations (before the SECURE Act) provided that if a trust was named as the beneficiary of a retirement account, the IRS would look or *see-through* the trust and identify its *individual* beneficiaries and thus treat the trust's *individual* beneficiaries as the *designated beneficiaries* of the decedent's retirement account. It was attempting to qualify for the *see-through trust* rules that caused the problem. I've covered those four basic *see-through trust* rules in the past and will not repeat them here, other than note one of the four requirements is that the trust beneficiaries had to be *identifiable*. There are two types of *see-through trusts*: (i) *conduit*; and (ii) *accumulation*.

Conduit See-Through Trust: This type of trust is not much of a problem. Only its present or current beneficiary is considered for implementing the *see-through rules*, and all other trust beneficiaries e.g., all trust remainder beneficiaries, vested or contingent, were ignored. With a *conduit see-through trust*, the trustee is required to promptly distribute any retirement funds that it receives as an RMD to the current trust beneficiary.

Example: My IRA names an irrevocable trust as its beneficiary. My son is the current beneficiary of that trust. The trustee is directed by the trust instrument to promptly pay all retirement distributions that the trustee receives to my son. Accordingly, the retirement distributions come into the trust and are promptly distributed to my son. This is a *conduit see-through trust*, and my son will be treated by the IRS as the designated beneficiary of my IRA.

Accumulation See-Through Trust: As the named suggests, this type of trust enables the trustee to accumulate retirement plan distributions that it receives, which means that either current or remainder beneficiaries might ultimately receive the retirement plan distribution. This is where the 'old' *see-through trust* rule became more problematic, or more accurately a concern of the IRS. That is because all potential trust beneficiaries who/which *might* someday receive a distribution from the trust would have to be 'counted' as an identifiable beneficiary. The real problem was that many trusts name a charity as an 'end' trust contingent remainder beneficiary if all other individual beneficiaries have died. A charity is not an *individual*. Accordingly, with a *accumulation see-through trust*, if it was possible that the charity *could* possibly receive a future distribution of accumulated retirement plan distributions to the trust that were accumulated by the trustee, then the trust would have a non-person trust beneficiary resulting in the IRA payable to the trust having to be emptied within 5 years of the IRA owner's death- even though the settlor named individuals as the first-in-line trust beneficiaries, and the named charity was only an after-thought.

Example: I name a trust as the beneficiary of my IRA. My son is the current trust beneficiary for his lifetime. The trustee is authorized to accumulate trust income, including any distributions that it receives from my IRA. The trust instrument provides that in the event my son dies, either while I am alive or after my death, my son's descendants are the lifetime remainder beneficiaries. The trust instrument goes on to provide that in the event of my son's death, and he leaves no surviving descendants, then the trustee is to distribute the trust's corpus to the American Red Cross, a 501(c)(3) charity. Because the charity is a potential beneficiary that might receive the accumulated retirement account distributions held in the trust, the trust is not treated as a *see-through trust* and the IRA must be emptied in distributions to the trustee within 5 years of my death. Even though the American Red Cross was added to the trust as an after-thought it, and it actually receiving a distribution of the trust's corpus was extremely remote, since I assumed either my son or his descendants would receive all of the

trust assets after my death, the trust did not qualify as a *see-through trust* simply due to the presence of a non-individual, i.e., charity, named contingent remainder beneficiary.

SECURE Act Final Regulations: The Final Regulations provide examples that now indicate that with an *accumulation see-through trust*, the search for the identifiable trust beneficiaries will stop after the primary and secondary beneficiaries, both of whom will be treated as the *designated beneficiaries* of the decedent's retirement account that is made payable to the decedent's trust. More remote contingent beneficiaries named in the trust instrument will be ignored. [Regulation 1.401(a)(9)-4(f)(3).]

Regulation 1.401(a)(9)-4(f)(3)(i)(B) counts: "*any beneficiary of an accumulation trust that could receive amounts...that were not distributed to beneficiaries described in paragraph (f)(3)(i)(A)* [primary beneficiaries.]" This includes all other remainder beneficiaries, but only applies to accumulation trusts. These countable beneficiaries *are restricted to secondary beneficiaries* as are described in paragraph (f)(3)(ii)(A). That paragraph limits the application of paragraph (f)(3)(i)(B) to count only secondary beneficiaries by stating that "*any beneficiary of an accumulation trust who could receive amounts...solely because of the death of another beneficiary described in paragraph (f)(3)(i)(B)...is not treated as having been designated of the employee under the plan.*"

This obtuse Regulation language limits the scope of paragraph (f)(3)(i)(B) to secondary beneficiaries of the trust, meaning only those who come after the current trust beneficiary.

Example: My IRA names a trust as its beneficiary. The trust is to provide for my son for his lifetime, with the trustee possessing discretion to accumulate trust income, including any retirement account assets distributed to the trust. Upon my son's death, I name my brother Richard as the secondary beneficiary for his lifetime. Upon my brother's death, I then name my brother's daughter Kate as the contingent beneficiary of the trust. If Kate predeceases either my son or my brother, and she leaves descendants, the trust is to distribute all of its corpus to Kate's descendants, per stirpes. In the event Kate dies without any surviving descendants, then the trustee is to distribute the trust corpus to the American Red Cross. This is an *accumulation see-through trust*. Under the Final Regulations, both my son and my brother will be treated as identifiable *designated beneficiaries* under the trust to comply with the *see-through trust* rules. My niece Kate, and Kate's descendants, if any, and the American Red Cross will all be ignored when the beneficiaries of my trust are identified. Under the 'old' rules, the presence of the American Red Cross as a potential contingent beneficiary would have caused the trustee to have to empty the trust within 5 years of my death, even if my son had been classified as an eligible designated beneficiary whose life expectancy could have controlled the RMDs from the IRA. Now, the

IRA payable to the trust will be emptied in 10 years, or longer if my son is an *eligible designated beneficiary* due to a disability or chronic illness.

Conclusion: With the new Final Regulations, with an *accumulation see-through* trust, only the current trust beneficiary and the secondary beneficiary or beneficiaries (who takes when the current trust beneficiary no longer is living or is ineligible to receive distributions) are counted when implementing the *see-through trust* rules. This is a positive result since it narrows the group of trust beneficiaries who must be identified for the see-through rules.