RMDs- New Insight from the IRS

Take-Away: Naming a trust as the designated beneficiary of an IRA creates considerable confusion since it triggers multiple factors and conditions set-forth in the Tax Code.

Background: Naming a trust as the beneficiary of a retirement account often strikes terror in the heart of an advisor. Naming the trust as beneficiary under an IRA beneficiary designation is not much of a challenge. Rather, it is understanding that the required minimum distribution (RMD) rules that will apply when the trust is named are complex, confusing, and often filled with distracting titles (or concepts) like *see-through trusts,* the *still-working exceptions,* and *ghost life expectancy.* Consequently, it is with dread I read any time the IRS comes out with yet another 'explanation' of how the RMD rules work when a trust is named as the beneficiary of the decedent's retirement account. Such was the case recently when the IRS issued yet another private letter ruling attempting 'clarify' the RMD rules when several IRAs were paid to the decedent's trust.

Private Letter Ruling 202506004 (February 7, 2025)

Facts: The decedent, let's call him Irv for simplicity, died after his required beginning date (RBD). Irv had created a revocable trust, and he designated that trust as the primary beneficiary of his multiple IRAs. The beneficiaries of Irv's trust were several named individuals, and charities. On Irv's death, the trustee of his trust was directed to divide the remainder of the trust property into specific percentage shares, first among several individuals (called the *non-charitable share*) and the remaining percentage amount to several charitable organizations to be selected by the trustee (the *charitable share.*) Irv's trust probably did not qualify as a see-through trust [IRC 401(a)(9)(H)(v)] because it was not irrevocable until Irv's death.

Trustee PLR Proposals: In seeking an expensive private letter ruling (PLR) the trustee asked:

Charitable Share: After Irv's death the trustee would form a 501(c)(3) private foundation. The trustee proposed to take a lump sum of cash from Irv's IRAs and pay that amount to the private foundation within the same taxable year.

Non-Charitable Share: To the extent that the value of the decedent's IRAs exceeds the value of the *charitable share* to be funded with cash from Irv's IRAs, the trustee proposed to transfer the amounts remaining in the inherited IRAs to one or more of the named individuals, executed in trustee-to-trustee transfers for the benefit of those named individuals using inherited IRAs. Each of these inherited IRAs would be set-up by the trustee, titled in Irv's name 'for the benefit of' each of the named individuals. After those custodian-to-custodian transfers, the trustee would then terminate Irv's trust in the same taxable year.

Requested Rulings: The questions that the trustee had, prompting its request for a private letter ruling from the IRS, dealt with: (i) who is responsible for the income tax?; and (ii) what are the RMD obligations? Answering these questions led to several IRS opinions, a couple of which were surprising.

Income Tax Deduction: The IRS said that Irv's trust will be entitled to an income tax deduction under IRC 642(c)(1) equal to the gross income from the lump sum distribution of cash it receives from the IRAs to the extent that the cash is distributed to the private foundation in the same taxable year.

Trustee-to-Custodian Transfer: The IRS said that the transfer of Irv's IRAs to inherited IRAs established for each of the named individual beneficiaries would not result in taxable payments under IRC 408(d)(1). Thus, the transfer from Irv's IRA custodian directly to the newly created inherited IRA custodians would not be a taxable distribution. In effect, this skips the steps of (i) a transfer into the Irv's trust (the original designated beneficiary), and (ii) then from Irv's trust to the inherited IRAs created by the trustee for each of the named individuals. Thus, the custodian-to-custodian IRA transfers are nonreportable transfers.

This is an important change from what was believed to be the correct procedure, which was a payment from the IRA to Irv's trust (taxable income) without the ability of the non-spouse individual beneficiaries' ability to then rollover the amount paid into Irv's trust to their own inherited IRAs (only spouses can do a rollover of an inherited IRA.) This would have caused the trustee to pay the income tax liability when the IRAs were paid to the trust.

Key Point: This PLR apparently permits the trustee to avoid having to pay income taxes when the IRA is paid to the trust, instead by skipping the trust completely and having the IRA custodian pay the IRA directly to inherited IRAs that the trustee creates for each of its individual beneficiaries. The trustee never receives the IRA proceeds with his 'let's just skip the trust' strategy.

Not a *Transfer:* The IRS also said as to the division of Irv's IRA and the custodian-to-custodian transfer into the inherited IRAs for each of the individual beneficiaries, that such *transfer* would not be included within the meaning of IRC 691(a)(2). The individual beneficiaries of the inherited IRAs will be responsible for their own income taxes on their RMDs, and Irv's trust will not be responsible for income taxes or penalties if the individual beneficiary fails to take his/her RMD. Each of these individual beneficiaries might also be able to claim an IRC 691(c) income tax deduction if federal estate taxes were paid on Irv's IRA account balance at the time of his death. **What this PLR tells us is that individual beneficiaries who inherit IRAs through a trust will be personally liable for RMDs and income taxes, not the decedent's trust.**

RMDs: The IRS also said that each of the individual beneficiaries can take RMDs from their inherited IRAs (resulting from the custodian-to-custodian transfer) for Irv's remaining life expectancy (or his *ghost life expectancy*) using the IRS actuarial table, and that each inherited IRA will be independent of any RMDs taken by the other individual beneficiaries from their respective inherited IRAs.

See-Through Trust Rule: This private letter ruling seems to imply that Irv's trust remained revocable on Irv's death, thus making it a non-designated beneficiary and thus subject to Irv's remaining life expectancy, i.e., it did not qualify as a see-through trust. When a trust does not qualify as a see-through trust, it is treated as a non-designated beneficiary. Because Irv died after his RBD, distributions to this non-designated beneficiary must be made over Irv's single life expectancy, set in the year of his death, and reduced by 1.0 for each subsequent year. Had the trust qualified as a see-through trust, distributions would have been calculated over the single life expectancy of the oldest trust beneficiary. Yet the IRS did not address whether it is a see-through trust, or not.

Mistaken Tax Code Reference: Apparently the trustee had requested this private letter ruling in reliance on both IRC 402(c) and IRC 408(d)(1). The IRS did not catch the mistake that IRC 402(c) [which deals with rollovers] applies only to qualified plans and not to IRAs. The IRS did not clarify in its response that IRC 402(c) did not apply (it was silent on its inapplicability); that omission does not generate a lot of confidence in the soundness of this private letter ruling.

Conclusion: This private letter ruling provides some insight and guidance into how beneficiary designations might be structured when a trust is named as the beneficiary of a decedent's IRA. The questions ask and the scope and complexity of the IRS's response, does suggest however that it would have been much easier for Irv to have set up the private foundation during his lifetime, and directly name the private foundation as the beneficiary one of Irv's IRAs, and that Irv could have simply named the individuals directly as the beneficiaries of his remaining IRAs, all without incurring the expense of the need to ask for a private letter ruling. [If Irv was worth $10 million or more, the cost of this private letter ruling was $43,700!]

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