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IRS PRIVATE LETTER RULING CLARIFIES IRA BENEFICIARY DESIGNATION RULES

1 The IRA owner had elected to receive payments over the joint life expectancy of herself and the first IRA beneficiary and to recalculate her life expectancy annually, as provided under the relevant IRS regulations, including Section 1.401(a)(9)-1, Q&A E-8(b) of the proposed regulations. [11251] September 16, 1999 TO: PENSION OPERATIONS ADVISORY COMMITTEE No. 42-99 PENSION MEMBERS No. 33-99 AD HOC COMMITTEE ON IRA BENEFICIARY DESIGNATION RE: IRS PRIVATE LETTER RULING CLARIFIES IRA BENEFICIARY DESIGNATION RULES

_____ The Internal Revenue Service recently released a private letter ruling that clarifies the application of the required minimum distribution rules where an IRA beneficiary (herein the “first IRA beneficiary”) names his own contingent beneficiary (herein the “contingent beneficiary”) to receive distributions from the IRA after his death. Analyzing the specific facts presented in the private letter ruling, the Service concluded that the first IRA beneficiary may name a contingent beneficiary, who would be required to take payments in accordance with the required minimum distribution schedule established at the time benefits commenced, in accordance with Section 401(a)(9) of the Internal Revenue Code. In PLR 199936052, which is dated June 16, 1999, the Service addressed the following facts: An IRA owner died at age 71. The IRA owner named her only child (the first IRA beneficiary) and elected to receive required minimum distributions from the IRA over the joint life expectancy of herself and the child. The IRA owner received minimum distributions for the year in which she attained age 70 ½ and for the following year, during which she died. The first IRA beneficiary will take distributions over his remaining life expectancy.1 The first IRA beneficiary sought clarification from the Service of the applicability of the required minimum distribution rules if he named a contingent beneficiary to receive the remaining balance in the IRA, if any, on his death and further sought a determination as to the applicability of federal estate tax rules. The Service ruled that although the first IRA beneficiary could name a contingent beneficiary to receive payments from the IRA after his death, the naming of that contingent beneficiary would not change the required minimum distribution schedule that was determined when benefits commenced. The Service stated that required minimum distributions must continue to be withdrawn at least as rapidly as under the method of distribution being used by the IRA owner. Code Section 401(a)(9)(B). The first IRA beneficiary, or after his death, the contingent beneficiary, would retain the right to accelerate distribution and withdraw assets from the IRA more rapidly than the required minimum distribution rules would require. The original IRA owner had named the first IRA beneficiary as her “designated beneficiary,” and “[o]nce distributions have begun, the designated beneficiary’s life expectancy is fixed and, in general, once the IRA owner dies, the designated beneficiary may not be changed.” Thus, “when the designated beneficiary’s

life expectancy is fixed at the time benefits commence such life expectancy is used after the designated beneficiary dies." See Section 1.401(a)(9)-1, Q&A E-8 of the proposed regulations. The first IRA beneficiary also asked the Service to clarify whether the IRA would be included in his estate upon his death for federal estate tax purposes in the event he dies before the IRA is exhausted, and if so, whether the IRA would be subject to a marital deduction should his spouse be named as contingent beneficiary. The Service ruled that at his death, the IRA is includible in the first IRA beneficiary's gross estate under Code Section 2041, because he possesses a general power of appointment over the IRA property. With respect to the marital deduction, Code Section 2056(b)(5) and Section 20.2056(b)- 5(f)(6) of the regulations provide, in part, that if a trust may be terminated during the life of the surviving spouse under her exercise of a power of appointment or by the distribution of the corpus of the trust to her, the interest passing in trust satisfies the condition that the spouse must be entitled to all the income in the property. If the first IRA beneficiary designates his spouse as sole beneficiary of the IRA in the event that he dies before the entire remaining balance in the IRA has been distributed to him, the spouse would have the right to accelerate distributions to herself up to the entire amount of the IRA balance. Thus, the IRA interest passing to the spouse would satisfy the requirements of Code Section 2056(b)(5) and Section 20.2056(b)- 5(f)(6) of the regulations and be eligible for the federal estate tax marital deduction. Russell G. Galer Senior Counsel Attachment Note: Not all recipients receive the attachment. To obtain a copy of the attachment referred to in this Memo, please call the ICI Library at (202) 326-8304, and ask for attachment number 11251. ICI Members may retrieve this Memo and its attachment from ICINet (http://members.ici.org).
