What We Need to Know About Taxes and Pooled Trusts

2021 National Conference on Special Needs Planning and Special Needs Trusts

Stetson University

Presented by:

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1

Presenter's Bio

Bradley J. Frigon

38 years practicing attorney • Focus in the elder law arena • Extensive experience across estate planning, estate and probate litigation, special needs planning, guardianship and conservatorship matters, Medicaid, and taxation • Nationally recognized expert in special needs planning and tax issues

Associations

- Past-President of the National Academy of Elder Law Attorneys (NAELA), NAELA fellow
- Appointed member of the Special Needs Alliance, special counsel for the Colorado Fund for People with Disabilities
- Fellow of the American College of Trust and Estate Counsel (ACTEC)
- Certified Elder Law Attorney (CELA)
- Member of the Council of Advanced Practitioners (CAP)
- Adjunct Professor at Stetson University College of Law
- Member of True Link Financial Investment Committee

2

2

Presenter's Bio

Peter J. Wall

Director of Fiduciary Services for True Link Financial • 20 years of professional trust administration - Focus in Elder Law & SNT planning

Prior to joining True Link Financial

- Developed and helped lead the BOK Financial Disability and Elder Trust Solutions division
- President of the Centennial Estate Planning Council
- Member of the Board of Directors for Easter Seals
- President of VSA Access Gallery
- Member of the Academy of Special Needs Planners

Special needs trusts, estate planning, taxation, and trust administration faculty member and presentations include:

- 2016, 2018, 2019, 2020 & 2021 Stetson National Conference on Special Needs Planning and Special Needs Trusts
- CBA 2012, 2014, 2015 & 2017 Elder Law Retreat
- 2013 National Down Syndrome Congress
- 2015 46th Annual Autism Society National Conference
- 2016 CBA Estate Planning Retreat
- 2017 & 2021 National Conference for National Guardianship Association
- 2019 Special Needs Alliance Conference
- 2019, 2020 & 2021 National NAELA Conference
- 2020 CA NAELA
- 2020 PFAC Annual Conference

3

3

PSNT Accounting Methodology

Omnibus Budget and Reconciliation Act 1993 (OBRA '93)

Omnibus Budget and Reconciliation Act 1993 (OBRA '93)

"for purposes of investment management of the funds, the trust pools these accounts"

"Pool" x 3

Legal (Master Trust Agreement/Joinder),
Administration (pooling of cash/investments = economy of scale), Tax

Can you pool 1st and 3rd Party sub-accounts together?

POMS SI 01120.25 - *"by law, each beneficiary must have a separate account, but the non-profit can pool these funds with the funds of other members of this communal trust"*

- Strict reading = only pool trusts created/authorized under 42 U.S.C. § 1396(d)(4)(c)
- However, not specifically prohibited
- Pooling separately may avoid tax complications:
  - Grantor Trust to Complex Trust upon death of beneficiary
  - Decedent proceedings
  - Etc.

4

4

PSNT Accounting Methodology

Unitization Overview

Beneficiary sub-account value adjusted daily for

- Joinder date/amount
- Sub-account transactions (distributions, receipts, etc.)
- Income items (dividends, interest)
- Capital gains (realized)
- Market value

Similar to mutual fund accounting and other general accounting principles
PSNT is **not** and mutual fund or investment offering

- Investment management is typically delegated to RIA under UPIA § 9
- *Restatement (Third) of Trusts* Prudent Investor Rule § 171
- **POMS SI 01120.25** - *"in some instances, the non-profit manager(s) may employ the services of a for-profit entity to manage some of the financial activities of the trust"*

5

PSNT Accounting Methodology

Why Daily Unitization?

Monthly Transactions

PSNT Value 2/1/2021	$1,090,000 (includes dividend and annuity receipt)
John Smith Sub-Account Value 2/1/2021	$240,000
Jane Doe Sub-Account Value 2/1/2021	$400,000
Bob Jones Sub-Account Value 2/1/2021	$400,000
XYZ Stock Total Dividend Paid 1/14/2021	**$50,000***
John Smith Annuity Receipt 1/15/2021	**$40,000**

**assume that dividend was for investors invested in XYZ stock from 1/1/2021-1/14/2021 and that ex-dividend date/record date corresponds accordingly*

6

PSNT Accounting Methodology

Why Daily Unitization?

Month-end Balances*

PSNT Value 2/1/2021	$1,090,000 (includes dividend and annuity receipt)
John Smith Sub-Account Value 2/1/2021	$240,000
Jane Doe Sub-Account Value 2/1/2021	$400,000
Bob Jones Sub-Account Value 2/1/2021	$400,000

Dividend Unitization Calculation (rounded)

John Smith Sub-Account (22% of PSNT)	$11,000
Jane Doe Sub-Account (39% of PSNT)	$19,500
Bob Jones Sub-Account (39% of PSNT)	$19,500

**assumes no market market movement*

7

7

PSNT Accounting Methodology

Why Daily Unitization?

Month-end Balances Post Dividend Calculation

PSNT Value 2/1/2021	$1,090,000 (includes dividend and annuity receipt)
John Smith Sub-Account Value 2/1/2021	$251,000
Jane Doe Sub-Account Value 2/1/2021	$419,500
Bob Jones Sub-Account Value 2/1/2021	$419,500

CAUTION!

- Dividend was paid on 1/14/2021
- John Smith annuity receipt received 1/15/2021
  - Did not materially participate at higher sub-account unitized value
  - John Smith received more of the dividend
  - Other beneficiaries received less of the dividend
- Areas affected: PSNT fee calculations, all beneficiaries' sub-account balances, reporting/statements, remainder person considerations
- **PSNT Counsel Tip: encourage PSNT to unitize daily**

8

8

PSNT Accounting Methodology

Why Daily Unitization?

Monthly Methodology

PSNT Value 2/1/2021	$1,090,000 (includes dividend and annuity receipt)
John Smith Sub-Account Value 2/1/2021	$240,000
Jane Doe Sub-Account Value 2/1/2021	$400,000
Bob Jones Sub-Account Value 2/1/2021	$400,000

Daily Methodology

PSNT Value 2/1/2021	$1,090,000 (includes dividend and annuity receipt)
John Smith Sub-Account Value 2/1/2021	$240,000
Jane Doe Sub-Account Value 2/1/2021	$425,000
Bob Jones Sub-Account Value 2/1/2021	$425,000

9

9

First Party PSNT

Grantor Trust

- **Grantor = Beneficiary**
- Beneficiary retains right to beneficial enjoyment of trust property, even if distributed purely by trustee's discretion

I.R.C. §§ 671 - 678

I.R.C. § 673(a)

"reversionary interest in either the corpus or the income therefrom if…the value of such interest exceeds 5 percent of the value of such portion."

I.R.C. § 677

"grantor shall be treated as the owner of any portion of a trust…whose income…may be distributed to the grantor…."

I.R.C. § 675

"grantor or any person [may] purchase, exchange, or otherwise deal with or dispose of the corpus or the income…."

10

10

First Party PSNT

Grantor Trust

- Sub-accounts taxable events flow out beneficiary
- Advantage - taxed at beneficiary's personal tax rate (if any)

2021 Simplified Federal Personal Income Tax Rates

Tax Rate	Single	Married, Filing Jointly
10%	$0 - $9,950	$0 - $19,900
12%	$9,951 - $40,525	$19,901 - $81,050
22%	$40,526 - $86,375	$81,051 - $172,750

2021 Simplified Federal Trust Income Tax Rates

Trust Taxable Income	Trust Tax Rate
$2,650 or less	10%
$2,650 - $9,550	$265 + 24% of excess over $2,650
$9,551 - $13,050	$1,921 + 35% of excess over $9,550
$13,051+	$3,146 + 37% of excess over $13,050

11

11

First Party PSNT

Hypothetical

First Party PSNT sub-account

Sub-account corpus $100,000	• Annual taxable interest = $500 • Annual ordinary dividends = $500
Beneficiary	• Receives SSI and Medicaid (no other income sources) Note: SSI is generally not taxable • No itemized personal deduction • 2021 standard deduction = $12,550
Conclusion	Beneficiary is not required to file a return, no federal income tax due

12

12

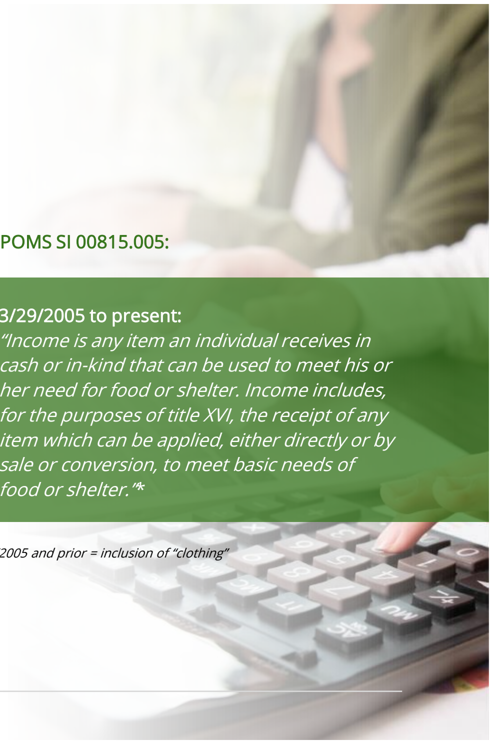
First Party PSNT

Income

Trust "income" is different than "income" for public benefits qualification

- **POMS SI 00815.001** - guidelines for what is **not** considered income
- **POMS SI 00815.001** & **POMS SI 00815.005** do not reference trust income (taxable or otherwise)
- Trust income may be retained by the trust at the discretion of the trustee

Counsel Tip:
Explain differences in "income" terminology to planning client



POMS SI 00815.005:

3/29/2005 to present:
*"Income is any item an individual receives in cash or in-kind that can be used to meet his or her need for food or shelter. Income includes, for the purposes of title XVI, the receipt of any item which can be applied, either directly or by sale or conversion, to meet basic needs of food or shelter."**

**3/8/2005 and prior = inclusion of "clothing"*

13

13

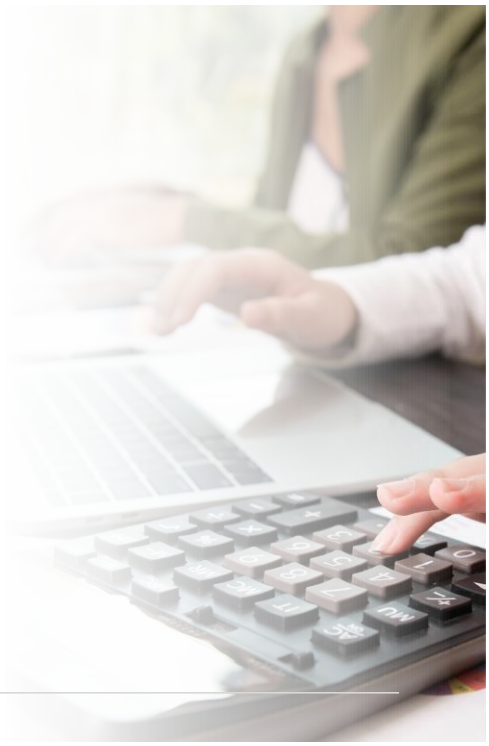
First Party PSNT

Capital Gains

If truly pooled (cash and investments), all beneficiary sub-accounts materially participate in gains/loss

Mutualized liquidity advantages

- Contributions/new joinders are investable as soon as deposit is made
- Decedent proceedings (overall cash position may satisfy remainderperson(s) position)
- Discretionary distributions
  - May alleviate need for liquidity trading
  - Quick access to cash
- Capital gains realization



14

14

First Party PSNT

Capital Gains

- PSNT investment holdings’ acquisition date and cost basis information is mutualized
  - NOT how long beneficiary has been in the pool; rather, how long the asset has been in the pool
- Capital gains are “realized” when assets are sold
- Short-term capital gains (assets held less than 1 year) are taxed at ordinary income rates or trust income rates
- Long-term capital gains (assets held more than 1 year) 2020 personal rates:

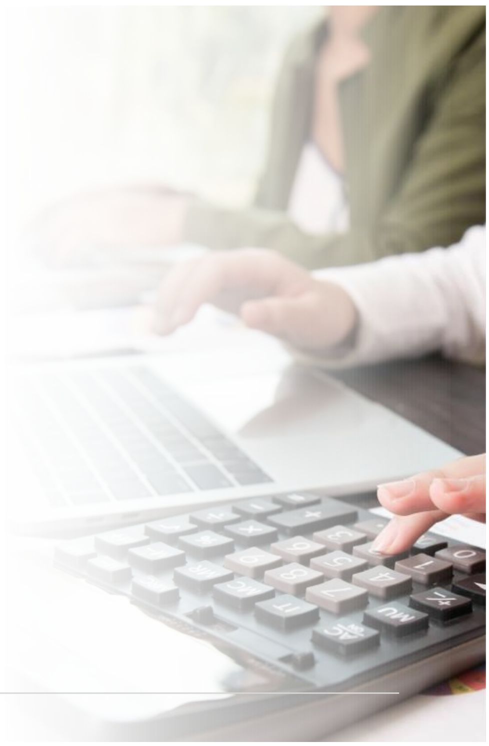
Long-Term Capital Gains	Beneficiary’s Income	Beneficiary + Spouse’s Income
0%	$0 - $40,000	$0 - $80,000
15%	$40,001 - $445,850	$80,001 - $501,600
20%	$445,851+	$501,601+

15

15

Capital Gains (general)

In-Kind Transfers



PSNTs are often asked to serve as successor trustee (pooled or non-pooled)

- Accounts come with embedded legacy capital gains
- Referrers/family members may be adamant about in-kind acceptance

Counsel Tip:
Consider the following hypothetical

16

16

Capital Gains (general)

In-Kind Transfers

Hypothetical (same assets):

- PSNT accepts appointment as successor trustee for Steve Smith
  - Transfers all assets in-kind into the pool
- Assets transferring in are identical in terms of ticker symbols (ABC Stock & XYZ Stock)
- Assets transferring are **not** identical in terms of cost basis and acquisition date
- Tax lot detail should appear as follows:

Asset	Acquisition Date	Total Cost Basis	Long-Term (LT) / Short-Term (ST) Gain/(Loss)	Sub-Account "Owner"
5 shares XYZ Stock	1/1/2021	$40,000	$30,000 (ST)	Steve Smith
10 shares XYZ Stock	9/1/2006	$25,000	$15,000 (LT)	All other PSNT sub-accounts
15 shares XYZ Stock	6/1/2001	$20,000	$20,000 (LT)	All other PSNT sub-accounts
5 shares ABC Stock	1/1/2021	$10,000	$10,000 (ST)	All other PSNT sub-accounts
10 shares ABC Stock	9/1/2006	$25,000	($5,000) (LT)	Steve Smith
15 shares ABC Stock	6/1/2001	$1,000	$19,000 (LT)	All other PSNT sub-accounts

17

17

Capital Gains (general)

In-Kind Transfers

Hypothetical (same assets):

PSNT's investment advisor rebalances overall PSNT holdings:
- Sells 1/1/2021 XYZ Stock tax lot
- Sells 9/1/2006 ABC Stock lot

Resulting tax ramifications:
- All PSNT sub-accounts realize proportionate $30,000 in short-term capital gains (taxed as regular income)
  - Should have only been attributed to Steve Smith
- All PSNT sub-accounts realize proportionate $5,000 in long-term capital losses
  - Should have only been attributed to Steve Smith

Issues:
- All PSNT sub-accounts are harmed proportionately by short-term gains in which they didn't materially participate
- Steve Smith is harmed as his sub-account was the only sub-account that historically materially participated in the capital loss
- Duty of impartiality

PSNT Counsel Tip: consider advising PSNT to hold in-kind transferred assets separate from the pool

18

18

Capital Gains (general)

In-Kind Transfers

PSNTs are often asked to serve as successor trustee (pooled or non-pooled)

- Accounts come with embedded legacy capital gains
- Referrers/family members may be adamant about in-kind acceptance
  - Should not be accepted into the pool (see prior Hypothetical)
  - Does the tax burden actually exist if the holdings are sold?
  - Note: almost never a reason to transfer an IRA in-kind

19

19

Capital Gains (general)

Hypothetical

First Party PSNT sub-account

Sub-account corpus $100,000	• $25,000 in long-term unrealized capital gains • Annual taxable interest = $1,500 • Annual ordinary dividends = $1,500
Beneficiary	• Receives SSI and Medicaid (no other income sources) Note: SSI is generally not taxable • No itemized personal deduction • 2021 standard deduction = $12,550
Conclusion	Beneficiary AGI is less than $40,000, no capital gains tax due (0% tax rate)

20

20

Capital Gains (general)

Hypothetical

HOWEVER: Long-term capital gains are includable in beneficiary AGI as follows (note: 2020 tax rates):

Beneficiary AGI:

$28,000 *(Line 11, Form 1040 (2020))*
(long-term capital gains + taxable interest + ordinary dividends)

**Note that SSI is generally not taxable income.*

Beneficiary Taxable Income:

$15,450 *(Line 15, Form 1040 (2020))*
($28,000 AGI minus 2020 standard deduction of $12,400)

Beneficiary Tax Due:

$1,660 *(Line 16, Form 1040 (2020))*
See IRS 2020 1040 Instruction Form, Tax Table

Conclusion: Tax due of only $1,660 may be prudent (0.83% of trust corpus) as a de minimis expense for ease of administration and portfolio considerations

Counsel Tip: Consider all facets of beneficiary's tax situation and/or consult with tax professional

Beneficiary Considerations

Elimination of Miscellaneous Itemized Deductions

- I.R.C. § 67 previously allowed for miscellaneous itemized deductions on personal returns if the following expenses exceeded 2% of beneficiary's AGI:
  - Employee business expenses
  - Tax preparation fees
  - Investment interest expenses
  - Grantor trust administration expenses (trustee fees, legal, accounting, etc.)
- Eliminated by 2018 Tax Cuts and Jobs Act (TCJA)
- Grantor Trust expenses flow out to beneficiaries just as taxable events
  - No longer deductible on beneficiary Form 1040
  - Note: may not have large impact as standard deduction was raised to $12,550 (single) and $18,800 (married filing jointly)

First Party PSNT

Tax Filing

I.R.C. § 6012(a)(4): Income tax return must be filed for every trust with gross income of $600 or over (regardless of the amount of taxable income)

26 CFR § 1.6012-3(a)(1)(ii): Form 1041 must be filed if trust produced at least $1 of taxable income or $600 of gross income

- Note: "gross income" would not apply to Grantor Trusts as all income flows out to beneficiary

26 CFR § 1.6012-3(a)(9): Alternative reporting requirements

26 CFR §1.671-4: Reporting requirements for Grantor Trusts

- Specific to trusts with one grantor/beneficiary or a limited number of grantors/beneficiaries
    - 26 CFR §1.671-4(b)(3): Requires income attributions among owners

Conclusion: No specific IRS guidance

First Party PSNT

Tax Filing

26 CFR §1.671-4(b)(2)(iii)(B)(1)

- Trustee must inform IRS that the Grantor is liable for income tax
- Trustee must provide Grantor information regarding trust income and expenses for the tax year

"Simplified" information may be sufficient under 26 CFR §1.671-4(b)(2)(iii)(B)(1)(ii)

Should include "the information necessary to take the items into account in computing the grantor's...income."

Issuance of Form 1099 to beneficiaries will not meet these requirements

Additional timing issues (1099s must be issued by Feb 1 of following tax year - many custodians subsequently adjust 1099s after Feb 1)

Grantor Tax Letter (see Appendix in materials)

First Party PSNT

Tax Filing

Form 1041 for every PSNT sub-account?

- Onerous
- Very costly (especially to low balance sub-accounts)
- Requires PSNT trustee to obtain TINs for every new joinder

PSNT counsel tip: Consider cost of filing individual 1041s for every PSNT sub-account when advising on tax reporting methodology

"Master" (a/k/a "Skeleton") 1041 for
PSNT U.S. Income Tax Return for Estates and Trusts

- Daily unitization is crucial
- Fulfills aforementioned IRS regulations
- Beneficiaries receive Grantor Tax Letters (GTLs)
  - GTLs may include potentially deductible items for beneficiary (e.g., medical expenses, trustee fees, etc.)
    Note: beneficiary should consult with their own tax professional for deductibility

PSNT counsel tip: Consider inclusion of such language on GTL (see Appendix)

Benefits

- PSNT trustee does not need to obtain TINs for every joinder
- Significant savings to PSNT sub-accounts
- Easy conversion process

Note: Requirements for state tax filings vary state-to-state

Third Party PSNT

Complex Trust or Qualified Disability Trust (QDT)

- Grantor = Someone other than the beneficiary
- Grantor cannot retain any interest (residual or otherwise)

I.R.C. §§ 661 - 663

Only one of the following need apply for complex trust status:

- Trust may accumulate income
- Trust may distribute corpus
- Trust may make distributions to charity

I.R.C. § 661	I.R.C. § 662	I.R.C. § 663
Complex trust deductions	Inclusion of amounts of income of beneficiaries	Other special rules

Third Party PSNT

Distributable Net Income

- **Trust Accounting Income (TAI):** deductions for amount that is required to be distributed
- **Distributable Net Income (DNI):** limits distribution deduction and tax-exempt income
  - May limit amount of taxable income that can flow out to beneficiaries
  - Measures greatest amount deductible due to beneficiary distributions
  - Characterizes income distributed for distribution deduction
  - Any taxable income undistributed to or for the benefit of the beneficiary may remain "trapped" in the trust and taxed at the trust level:

2021 Simplified Federal Trust Income Tax Rates

Trust Taxable Income	Trust Tax Rate
$2,650 or less	10%
$2,650 - $9,550	$265 + 24% of excess over $2,650
$9,551 - $13,050	$1,921 + 35% of excess over $9,550
$13,051+	$3,146 + 37% of excess over $13,050

Third Party PSNT

Distributable Net Income | Hypothetical

Third Party PSNT sub-account

Sub-account corpus $100,000	• Annual taxable interest = $5,000 • Annual ordinary dividends = $5,000

PSNT trustee has only distributed $5,000 to or for the benefit of the beneficiary

Beneficiary	$5,000 in taxable events potentially flow through and are taxed at beneficiary's tax rates
Trust	$5,000 in taxable events remain potentially "trapped" in the trust - **Tax due** of $829 ($265 + (24% of $2,350)

Third Party PSNT

Distributable Net Income

In general:

(Taxable Income) − (Net Capital Gains) + (Tax-Exempt Income Reduced By Expenses) = DNI

Third Party PSNT

Distributable Net Income

I.R.C. § 643(a)(3):

General rule = capital gains and losses are not included in DNI
- Allocated to principal
- Remainderperson consideration (see Uniform Principal and Income Act)

Exceptions where capital gains may be included in DNI
- Allocated to TAI
- Allocated to principal and "paid, credited or required to be distributed to any beneficiary…."
- Allocated to principal and "paid, permanently set aside, or to be used for [charitable] purposes…."

-- OR --

Capital gains may be included in DNI to the extent they are:
- Allocated to income
- Allocated to principal but treated consistently by the trustee on the trustee's books
- Allocated to principal but actually distributed to of for the benefit of the beneficiary

Only allowable if permitted by trust language or local law
- A/K/A/ "Power to Adjust"

PSNT counsel tip: Consider review of PSNT trust document and/or local law to ensure capital gains inclusion in DNI

Third Party PSNT

Distributable Net Income

Net Tax-Exempt Interest

Included in DNI: amount of tax-exempt interest reduced by expenses allocated to tax-exempt interest that would be deductible

Example

Beneficiary A's Third Party PSNT sub-account accrued $100 of tax-exempt interest	PSNT trustee's fees for the taxable year for Beneficiary A's sub-account totalled $40 as it was all allocated to the tax-exempt interest	Beneficiary A's DNI would include $60 of the net tax-exempt interest ($100 - $40)

31

31

Third Party PSNT

Qualified Disability Trust (QDT)

$4,300 (2020) additional exemption which would reduce the tax burden of taxable events "trapped" in the trust

Qualification requirements

42 U.S.C. § 1396p(c)(2)(B)(iv)
- Trust is irrevocable
- Sole benefit of the beneficiary with a disability
- Beneficiary is under the age of 65
- Beneficiary is disabled as **determined** by SSI/SSDI

Issues: beneficiary works or parental deeming rules

Trust must have simple or complex trust status (I.R.C. § 652 or 662)
- Note: this requirement therefore excludes First Party (Grantor) Trusts

32

32

Third Party PSNT

Qualified Disability Trust (QDT)

Pros	Cons
• Additional exemption of $4,300 to offset any "trapped" income	• Compressed trust tax brackets • Additional filing costs – Most likely would have to be filed separately from the PSNT Master 1041

Consider filing a sub-account as a QDT when:

- Trust does not distribute all income to or for the benefit of a beneficiary
  - Beneficiary may have 1st Party trust that is spending down first
  - Beneficiary has few discretionary distribution needs
  - Relatives of beneficiary are using the PSNT sub-account for inter vivos planning
- Trust sub-account has few deductions
- QDT exemption tax savings far exceeds cost of trust tax return preparation

PSNT counsel tip: consider review of existing Third Party PSNT sub-accounts that may benefit from QDT exemption

33

33

Third Party PSNT

Tax Filing

- I.R.C. § 6012(a)(4): income tax return must be filed for every trust with gross income of $600 or over (regardless of the amount of taxable income)
- 26 CFR § 1.6012-3(a)(1)(ii): Form 1041 must be filed if trust produced at least $1 of taxable income or $600 of gross income

"Master" 1041 for PSNT – U.S. Income Tax Return for Estates and Trusts

- Daily unitization is crucial
- Fulfills IRS regulations
- Beneficiaries receive Form K-1s
  - Form K-1s generally do not include potentially deductible items for beneficiary (e.g., medical expenses, trustee fees, etc.)
    - Beneficiary may rely on year end statements for such information
    - Note: beneficiary should consult with their own tax professional for deductibility

Note: Requirements for state tax filings vary state-to-state

PSNT counsel tip: Consider a review of beneficiary situs to ensure proper state tax filings

Benefits

- PSNT trustee does not need to obtain TINs for every joinder
- Significant savings to PSNT sub-accounts
- Easy conversion process

34

34

Third Party PSNT

65-Day Rule

- I.R.C. § 663
  - Trustee may elect to include a distribution made within 65 days of the new year in the prior year's deductions
  - Election is irrevocable after deadline (April 15)
  - If no return is due - a statement may be filed with the IRS office where the return would have been filed (26 CFR § 1.663(b)-2(a)(2
- Important for DNI calculations
- PSNT trustee should still make prudent discretionary distribution decisions

PSNT counsel tip: consider review with PSNT's tax professional annually to determine need for 65-Day Rule election

Third Party Revocable PSNT

Funded by someone other than the beneficiary

Grantor Trust for tax purposes

- Grantor (or their spouse) typically have remainder interest in the trust
  - Usually in case beneficiary predeceases Grantor
- Grantor (or their spouse) may retain the right to terminate the trust at any time (e.g., revocable)
- Grantor (or their spouse) has material interest in the trust

Master 1041

Note: can be combined with Master 1041 for Third Party PSNT

- Master 1041 can issue GTLs and K-1s
- Easier to separate from Third Party PSNT 1041
  - Unitization complications
  - Decedent proceedings (change to complex trust)

Pros

- Establishes relationship between all parties while grantor is still living
- *Inter vivos* planning

Counsel tip: consider inclusion of Third Party Revocable SNT/PSNT as planning option

Third Party PSNT

Trust Termination

At beneficiary's death, sub-account beneficiary is the named remainderperson(s)

Proportionate taxable events:

- Jan 1 through beneficiary DOD - beneficiary
- DOD - sub-account closure - remainderperson(s)
- Daily unitization is crucial

Unique circumstances:

- IRA liquidation (taxed as regular income)
- Unique Asset sale (e.g., residence, etc.)

PSNT notification may be delayed

- Daily unitization is crucial

Third Party PSNT

Trust Termination

Sale of assets

- Beneficiary sub-accounts are typically moved to "cash" to preserve principal for remainderpersons
- Non-pooled Complex Trusts typically do not receive a "step up" in cost basis of assets in the trust to beneficiary's DOD
  - May not need to transfer remainderperson assets in-kind to delay embedded capital gains
  - No sales may required due to mutualized liquidity of PSNT (constantly buoyed by new joinders, etc.)
  - IRS' position is fully considered as capital gains are always reported when assets are sold

PSNT notification may be delayed

- Daily unitization is crucial

PSNT counsel tip: have PSNT obtain remainderperson(s) Form W-9 before releasing funds

- Form W-9 also acts as an affidavit that remainderperson is not subject to backup withholding

Secure Act

Setting Every Community Up for Retirement Enhancement (SECURE) Act

Passed at the end of 2019, effective for all IRA inheritors Jan 1, 2020

- Most planners did not anticipate enactment
- Very little warning before passage

Eliminated traditional "stretching" of RMDs in favour of full withdrawal within 10 years of IRA holder's death

Exceptions (receive funds based on life expectancy):

- Beneficiaries with disabilities
- Beneficiaries who are "chronically ill"
- Beneficiaries who are fewer than 10 years younger than the IRA holder

Withdrawals are taxed as regular income

SNT may be designated as beneficiary

Creates a "see-through" trust

- Conduit Trust: IRA distributions to the trust pass to the beneficiary
  - Taxed at beneficiary (not trust) tax rates
  - Generally mandatory to be distributed which may negatively impact public benefits eligibility
- Accumulation Trust: IRA distributions may be retained or distributed to/for the beneficiary in trustee's sole discretion
  - May result in trapped income vis-a-vis DNI
  - Generally maintains beneficiary's public benefits eligibility

Secure Act

Setting Every Community Up for Retirement Enhancement (SECURE) Act

PSNT Opportunity

- Majority of wealth in U.S. in retirement vehicles
- RMDs are only "minimum" amount required for distribution - additional funds may always be taken to enhance the lives of beneficiaries
- Tax deferral is beneficial to beneficiaries with disabilities
- Impact in community

PSNT counsel tip: consider Inherited IRA offering for PSNTs

Counsel tip: consider PSNT organizations that offer Inherited IRA administration during planning process

Note: can be combined with Master 1041 for Third Party PSNT

- Ten year rule would apply
- Issue for PSNT?
  - Note: IRS has recently taken this issue under consideration and a clarification should be forthcoming

Clarified "Kiddie Tax" rules

- May have resulted in 37% tax rate for minor beneficiaries
- Minors now revert to filing at parents' tax bracket (assuming they are filing as dependents)

Thank you!

What We Need to Know About Taxes and Pooled Trusts

2021 National Conference on Special Needs Planning and Special Needs Trusts

Stetson University

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41

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42

42

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