

Using a Trusteed IRA to protect, preserve and control your IRA assets

Bank of America Trust Services — helping you simplify your life, give lasting meaning to your wealth, and prepare for whatever the future may hold.

Whether you're creating a trust as part of your own estate plan or serving as a trustee or executor for someone else, our focus is on what's important to you—your unique goals for today and the future. We are dedicated to providing the services that address your specific needs in the way that works best for you.

As the leading provider of personal trust services,¹ we are able to offer a broad array of specialized services through a nationwide network of local offices. It is all part of our commitment to providing an unmatched level of personal service and care to you and your family, wherever you may call home.

The first IRAs were created in 1975 and contained no more than that year's maximum contribution—just \$1,500. Decades later, through annual contributions of ever-larger permitted amounts, rollovers from employer plans, and investment growth, IRAs have become a major financial asset (sometimes the largest asset) for many IRA owners. Yet many IRAs are still held in the simple custodial IRA format designed for small accounts.

For an individual who has amassed a significant balance in an IRA or whose IRA constitutes a significant percentage of the owner's wealth, the solutions that worked in the past may no longer be the best way to structure that IRA. The Trusteed IRA can offer greater protection for this important asset during the owner's life (for example in case of the owner's disability) and an increased ability to control disposition of the IRA after the owner's death. When these goals are important, consider using a Trusteed IRA.

What is a Trusteed IRA and how is it different from a “regular” IRA?

A Trusteed IRA is exactly the same as a “regular” IRA except that the account assets are held in a trust rather than a “custodial account.” The IRA provider—the financial institution that administers the IRA—serves as the trustee of the account, rather than as a “custodian.” Under the Tax Code, both types of IRAs are considered identical.

Most IRAs are in the form of custodial accounts with the IRA provider serving as custodian. The duties of the custodian of IRAs are:

- Holding the account assets.
- Keeping track of deposits, distributions, and investment changes.
- Reporting to the IRA owner regarding the IRA investments.
- Filing required tax reports with the IRS.

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Are Not FDIC Insured	Are Not Bank Guaranteed	May Lose Value
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With a Trusteed IRA, the bank or trust company holds the IRA assets as trustee rather than as custodian. In addition to all the same duties performed by a custodian, the trustee can assume additional responsibilities if requested to do so by the IRA owner:

- The trustee can have investment responsibility for the account, or can take investment directions from the IRA owner or a designated advisor. A custodian never has investment responsibility.
- The trustee can disburse funds for the benefit of the IRA owner, when authorized to do so by the owner. For example, paying the owner's bills directly if the owner is incapacitated. An IRA custodian cannot do this.
- The trustee can continue to carry out the IRA owner's instructions after the IRA owner's death, restricting the rate at which the beneficiaries receive access to the funds, subject to "required distributions." An IRA custodian cannot do this because beneficiaries of a custodial IRA have unlimited access to the inherited account.

IRAs generally must pay out a "required minimum distribution" (RMD) each year after the owner's death, and also, in the case of a traditional IRA, during the IRA owner's life after age 70½. Failure to pay out the RMD results in a substantial excise tax of 50% of the RMD that was not withdrawn. The trustee will compute and pay out that RMD each year as part of its duties. A custodian does not do this, leaving the IRA owner vulnerable to the excise tax when illness or any mishap causes failure to take the RMD.²

These and other features of the trust format lead to several potential advantages that the Trusteed IRA has over a custodial IRA. IRA owners who adopt Trusteed IRAs are usually seeking greater control after death, assistance in the event of disability, and possible protection of beneficiaries from creditors' claims.

Advantages of Trusteed IRAs

1. Control distributions after the owner's death

When an IRA owner dies, the account passes to his or her beneficiary. Under current tax law, the beneficiary of an IRA can continue the tax-deferred (or tax-free, in the case of a Roth) status of the IRA, by taking annual distributions from the account gradually over his or her life expectancy. The IRA owner may want his or her beneficiary to take advantage of this so-called "life expectancy" or "stretch" payout option. But what if the beneficiary doesn't see the advantage of that approach and would rather just take an immediate lump sum distribution of the entire account?

With a custodial IRA, the moment the owner dies, the beneficiary has complete and unlimited access to the account. For example, if a custodial IRA is left to a 25-year-old grandchild, the grandchild could withdraw it gradually over his or her life expectancy or he or she could cash out the account immediately and spend it (or spend what's left after paying the income taxes).

With a Trusteed IRA, the IRA owner can assure that the beneficiary will not cash out the account prematurely, by giving the trustee control over when distributions are made to the beneficiary. The trustee must pay to the beneficiary the annual RMD based on the beneficiary's life expectancy. Beyond that, the IRA owner specifies what additional distributions, if any, the beneficiary will receive. For example, the IRA owner could specify that the beneficiary will receive additional distributions for support or education at the trustee's discretion.

Contrast with custodial IRA

Although a custodial IRA generally cannot, itself, have a limited payout schedule for beneficiaries, the IRA owner could have his or her lawyer draft a separate trust instrument that would contain the restrictions the IRA owner wishes to place on the beneficiary's access to the funds. The IRA owner would then name that separate trust as beneficiary of the custodial IRA. This approach (custodial IRA payable to a separate trust created by the IRA owner) can accomplish the same results as the Trusteed IRA.

The IRA payable to a separate trust approach has two potential weaknesses and one potential strength compared with a Trusteed IRA:

- **Legal fees (potential weakness):** To prepare the separate trust approach, the IRA owner must pay a legal fee to have the separate trust drafted by a lawyer. While the IRA owner should expect to pay his or her legal advisor for estate planning advice even in connection with using a Trusteed IRA, it is probable that the fees for drafting a separate trust to be named as IRA beneficiary would be higher than the fees for reviewing and advising regarding adoption of a Trusteed IRA.
- **Risk of qualification as a see-through trust (potential weakness):** If the purpose of the trust is to assure that the beneficiary takes advantage of the "life expectancy payout method," the separate trust named as IRA beneficiary must meet numerous IRS requirements to qualify as a "see-through trust." Not all estate planning advisors are experienced in drafting trusts to meet these requirements. If the trust named as beneficiary does not qualify as a see-through trust, the IRA will have to be distributed much more rapidly after the owner's death than would otherwise

be the case. The risk of not qualifying as a see-through trust (and therefore forfeiting potential deferral) does not exist with a Trusteed IRA, because the trust is, itself, an IRA. No separate see-through trust is needed.

- **Ability to restrict beneficiaries' access (potential strength):** If desired by the IRA owner as part of his or her estate plan, a separate trust named as beneficiary can hold and retain IRA distributions — even RMDs — under the control of the trustee, for protection of the beneficiaries. A Trusteed IRA cannot do this.

2. Control disposition after the beneficiary's death

Some IRA owners want to be sure that, if there is any money left in the inherited IRA when the original beneficiary dies, that money will pass to the owner's chosen successor beneficiaries, not to new beneficiaries chosen by the first beneficiary. This can be particularly important for individuals who want to provide for both a current spouse and children from a prior marriage. This goal is easily accomplished with a Trusteed IRA. With a custodial IRA it is impossible to do this, unless the IRA is left to a separate standalone trust.

3. Anticipating possible disability

The IRA owner, thinking ahead, will anticipate his or her possible future disability resulting from advanced age or illness. It is advisable to prepare for that eventuality by (1) nominating one or more persons or institutions to manage the individual's finances, (2) setting up a legal mechanism for the chosen person or institution to carry out that responsibility, and (3) setting the standards that person or institution should follow.

With a Trusteed IRA, the IRA trust document can fulfill all of these requirements with respect to the IRA assets. The IRA trustee can assume responsibility for paying the IRA owner's expenses and bills directly from the IRA if requested to do so by the IRA owner or when it learns that the IRA owner has become disabled.

If the owner of a custodial IRA becomes disabled, the custodian cannot step in and assume greater financial responsibilities. The custodian could only respond to directions from either the holder of a power of attorney or a legal guardian or conservator in order for IRA funds to be used for the incapacitated IRA owner's benefit and in order for the RMD to be distributed.³ If the disabled IRA owner does not have a current power of attorney in place, expensive and lengthy court proceedings could be required to get a legal guardian or conservator appointed before the IRA funds could be used for the owner's benefit.

4. Concern about creditors of the beneficiary

During the IRA owner's lifetime, the IRA may have the protection of various federal and state laws designed to prevent creditors of the IRA owner from seizing the account to pay debts. Once the IRA owner dies, and the beneficiary owns the inherited account, this protection may be reduced or lost. For example, a recent Supreme Court case ruled that the bankruptcy exemption allowed for "individual retirement accounts" protects the IRA during the original owner's life, but expires upon his or her death. The inherited IRA is therefore an asset available to the beneficiary's creditors if the beneficiary suffers bankruptcy.

Generally, assets in a so-called "spendthrift trust" cannot be taken by the creditors of the trust beneficiary. Therefore if the IRA owner is concerned about potential creditors of his or her chosen beneficiary, the IRA owner should consider leaving the IRA in a protected spendthrift trust arrangement. There are two ways to accomplish this.

One is for the IRA owner to have his or her lawyer draft a spendthrift trust for the benefit of the intended beneficiary, then name that trust — rather than the individual — as beneficiary of the IRA.

The other is to use a Trusteed IRA with a restricted payout. Assuming the Trusteed IRA contains a "spendthrift clause" (most do), the beneficiary's creditors generally cannot access the IRA. They could try to seize IRA distributions as they are received by the beneficiary, but they cannot, under existing laws as operated in most states, go after the IRA directly.

Note: *If you are concerned about potential exposure to creditors' claims for either yourself or your chosen beneficiary, you need to consult a lawyer who is expert in "asset protection planning." The brief general statements here cannot cover the many complexities of this subject.*

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Other factors to consider

A Trusteed IRA is not the right solution for everyone. Two limitations in particular are cited as reasons why a particular individual would not use a Trusteed IRA: cost and the fact that required distributions must be paid to the beneficiary.

Cost

Because the trustee of a Trusteed IRA has greater responsibilities than the custodian of a custodial IRA, the annual fee of the IRA provider will normally be higher for a Trusteed IRA than for a custodial IRA. Here are three points to consider regarding this factor:

- The IRA owner needs to evaluate whether the advantages of the Trusteed IRA are worth the investment.
- If the IRA owner is already paying the financial institution for investment management with respect to a custodial IRA, the cost increase may be minimal or nonexistent to convert the account to a Trusteed IRA.
- Normally a Trusteed IRA format is not suitable for smaller accounts.

Required distributions must be paid to the beneficiary

As noted, the Trusteed IRA allows the IRA owner to prevent the beneficiary from simply cashing out the inherited account immediately upon the owner's death. However, even with a Trusteed IRA, the beneficiary will be receiving some distributions from the account that are outside the IRA owner's or trustee's ability to prevent. Specifically, the tax law requires that the beneficiary receive the RMD each year after the owner's death. This required distribution must be distributed each year.

The RMD issue is not a problem if all the IRA owner wants to do is ensure that the beneficiary takes advantage of the stretch or life-expectancy payout. However, if the owner wants the trustee to be able to hold back the RMDs and avoid passing them out automatically to the beneficiary, then the Trusteed IRA, by itself, can not accomplish the owner's goal.

- **Certain disabled beneficiaries:** A common situation in which this presents a problem is the disabled beneficiary for whom the IRA owner wants to leave the IRA in a "supplemental needs trust." Under a supplemental needs trust, the trustee has full control of the funds and uses them to supplement benefits the disabled beneficiary is receiving under means-tested government programs. If IRA payments are paid outright to the beneficiary, the payments will count as "income" or "assets" of the beneficiary and he or she may lose his or her qualification for the government benefits. Thus, a supplemental needs trust must give the trustee the power to hold back RMDs from the beneficiary.

Because Trusteed IRA RMDs must be distributed annually, a Trusteed IRA cannot be a supplemental needs trust. To leave IRA assets in a supplemental needs trust, the IRA owner would need to have his or her attorney prepare a separate supplemental needs trust and name it as beneficiary of the IRA.

- **Beneficiary who cannot suitably manage any funds:**

The same would be true in any situation where the IRA owner does not want the chosen beneficiary to have outright control of any of the IRA funds—for example, because the beneficiary does not have the capacity to handle money responsibly. If the IRA owner does not want the beneficiary to receive even the annual RMD, the IRA owner must use a separate trust and name it as beneficiary of the IRA.

Potential changes in the law

In selecting a Trusteed IRA or naming a beneficiary for any type of IRA, the IRA owner is usually relying on certain assumptions about what the tax laws and other laws provide. These assumptions are based on today's laws. Whatever plan or IRA format the IRA owner chooses, he or she must periodically check to make sure those assumptions are still valid—tax laws and other laws do change.

For example, periodically, various congressmen and others have proposed changes that would replace the life-expectancy payout with a faster required payout in most cases. There is no way to predict whether any of these proposals will ever be enacted, but most proposals would not affect the accounts of deceased IRA owners. However, living IRA owners who are counting on the "stretch" (life expectancy) payout as part of their estate plan would have to review their plans. Bank of America's Trusteed IRA is fully amendable and revocable as long as the IRA owner is living, enabling the IRA owner to make changes as needed to reflect changing laws, family circumstances, or goals.

A Trusteed IRA can offer greater protection for the IRA during the owner's life (for example in case of the owner's disability) and an increased ability to control disposition of the IRA after the owner's death.

Examples

Here are situations when an individual IRA owner might consider using a Trusteed IRA.

Spendthrift protection

Arthur wants to leave his IRA to his grandson Billy, age 21. Since Billy's support and education have been provided for by his parents, Arthur feels this inherited IRA should be preserved as a tax-deferred retirement plan for Billy, with the funds professionally invested for Billy's benefit. Arthur wants Billy to receive the annual RMD, and not to take out any additional funds from the account unless the trustee agrees that such additional distribution is advisable. Arthur places his IRA funds in a Trusteed IRA for Billy's benefit. Billy will not be able to unwisely cash out the account when Arthur dies; he will receive control gradually, through annual RMDs and, if appropriate, additional distributions in the trustee's discretion. Arthur knows he must keep an eye on tax law changes in Washington. If the "life expectancy payout" option is taken out of the Tax Code, Arthur might name a separate trust for Billy as beneficiary of his Trusteed IRA as the best way, under the circumstances, to give Billy only gradual rather than immediate access to the IRA funds. Meanwhile, until (if ever) that change in the law occurs, the Trusteed IRA achieves Arthur's estate planning goal and provides additional benefits during Arthur's lifetime such as professional investment management and disability protection.

Possible future disability

Grace recently retired and is structuring her assets and her estate plan for a hopefully long and happy retirement. With the help of her estate planning attorney she has adopted a will, living trust, and durable power of attorney. Turning her attention to her substantial IRA, she is concerned about how funds in this account will be handled if she becomes unable to manage her affairs. The will she signed has no effect on anything until after her death. Her living trust is set up to manage her assets, but IRA assets cannot be placed in a living trust during the owner's life. That leaves the durable power of attorney as the only instrument that could be used to manage IRA assets and make withdrawals to pay her bills in case of incapacity. But durable powers of attorney can be problematic—for example, the rights and duties of the holder of a power or attorney are not well settled in the law. Since her IRA is very substantial, and the financial institution where she keeps the IRA is also where her financial advisor is (who is very familiar with her family and finances), she adopts a Trusteed IRA. Now the trustee of the Trusteed IRA can respond directly to her needs in case of disability, instead of having to rely on the holder of a power of attorney.

Providing for a spouse and children from a prior relationship

George is married to Gina and has two children from a prior relationship. George wants to leave his IRA primarily for Gina's lifetime use. He wants her to receive the annual RMD, plus additional amounts (if any) needed (in the trustee's judgment) for her health and support. He is concerned, however, that upon Gina's later death, if there is still money in this IRA, it should pass to his children, rather than to Gina's relatives. George adopts a Trusteed IRA because he can specify how he wants his beneficiary(ies) to receive payments from the account after his death. If George used a custodial IRA with Gina as beneficiary, and Gina later died while there was still money in the account, that money would pass to Gina's chosen beneficiaries or heirs, not to George's children.

Creditor protection

Janet wants to leave her IRA to her son Louis. Louis is in the construction business and she feels he has exposure to lawsuits. Janet wants Louis to have this money, but at the same time she wants to give it some protection from potential future lawsuits. For total protection of the asset from any creditor of Louis, she would have to tie up the asset permanently in a spendthrift trust. She doesn't want to go that route, because Louis so far has avoided business problems and she really wants him to get the benefit of the money. But if she simply names him as outright beneficiary and he gets sued shortly after her death, the whole account might be lost. To compromise her conflicting goals, she uses a Trusteed IRA. Louis will get the RMD every year, so he will have funds from the account. But the rest of the account will remain safe from his creditors in the Trusteed IRA until it has all been paid out gradually over his life expectancy.

Is a Bank of America Trusteed IRA right for you?

Bank of America* is one of the few financial institutions that offers a Trusteed IRA. You may want to consider a Bank of America Trusteed IRA if you:

- > Have a substantial portion of your net worth held in an IRA.
- > Want to do what you can to see that you and your family have the assistance you need should you become incapacitated.
- > Are not certain that a beneficiary will be able to manage the funds wisely, use them as you intend, or recognize and avoid individuals who may be looking to take advantage of them.
- > Want to preserve continuity and direct how the IRA assets you leave behind are distributed.
- > Have children from a previous relationship and want to provide for them as well as your spouse.
- > Have a spouse who is not a U.S. citizen.

Bank of America Trust Services works closely with your relationship manager — who knows you, your needs and your goals for your wealth. Together, we focus on your unique situation, helping you identify trust solutions that align with your priorities and integrate them into your overall estate and wealth management plans.

To find out more about Bank of America Trusteed IRAs and the ways we can help you simplify your life and create lasting meaning for your wealth, reach out to your relationship manager.

* Trust and fiduciary services are provided by Bank of America, N.A., Member FDIC and wholly owned subsidiary of Bank of America Corporation (BofA Corp.).

¹ Spectrem Group, "2018 Comprehensive Bank Trust Update," November, 2018.

² Although all IRA custodians must calculate your RMD, some offer a service that allows the IRA owner to direct the custodian to automatically distribute the RMD each year.

³ Unless automated distribution service is in place.

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