Grace Global Alliance

An Independent Association of Christian Churches & Ministers

Stretch IRA Concepts
Generational Planning
Tax Year 2017

Prepared for:

Grace Global Alliance
Ministers & Churches

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June 20, 2017

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The Basics of Stretch IRAs

One major benefit of a traditional IRA[1] is that there is no federal[2] tax on growth in the account until the funds are distributed. This deferral of taxes generally allows for faster growth than would be possible if taxes had to be paid each year. Federal law does not allow this tax-deferral to continue forever; certain mandatory distributions (known as Required Minimum Distributions, or RMDs) must be made from these accounts once the owner reaches a specified age.

For traditional IRAs, distributions must begin no later than April 1 of the year following the year the owner reaches age 70½. Funds distributed from the account are generally taxable as ordinary income in the year received. Failure to make the minimum distributions when required can result in a significant income tax penalty.

The Stretch IRA - Extending the Period of Tax-Deferral

The term "stretch IRA" refers to a wealth transfer strategy that seeks to extend the period during which the assets in the IRA continue to grow tax-deferred. The stretch IRA concept is most often of interest to those who do not need extra income or those who wish to leave a legacy to their heirs in an income tax-efficient manner.

To begin, an IRA owner names a spouse or another (usually younger) person such as a child or grandchild, as the account beneficiary. Then, only the legally required, minimum distributions, (the RMDs), are taken from the account each year. Under IRS regulations, the methods used to calculate the RMDs can effectively extend the period over which the assets may be distributed.

The Pros and Cons of Stretch IRAs

Stretch IRAs have potential benefits as well as potential risks:

- **Benefits.**
    - **Income for life:** A stretch IRA has the potential to provide lifetime income to a chosen beneficiary or beneficiaries.

[1] The term "traditional IRA" includes SIMPLE IRAs and SEP IRAs.

[2] The discussion here concerns federal income tax law. State and/or local tax law may differ.

- **Minimize tax liability:** The income tax bite may be lessened by taking smaller distributions over a period of years, rather than as a single, large lump sum.

- **Continue tax-deferred growth:** Extending the period over which distributions are made continues the benefits of tax-deferred growth, potentially increasing the wealth that can pass to the beneficiaries.

- **Risks.**

  - **Beneficiary may die early:** A beneficiary may not live to normal life expectancy.

  - **Tax laws may change:** Tax laws or regulations may change, to the detriment of an IRA owner and/or beneficiaries.

  - **Poor investment returns:** Investment losses and inflation can both erode, or even eliminate, the value of future IRA distributions.

Spousal Beneficiary and a Single Inherited IRA

An IRA owner, age 68, makes his spouse, age 62, the sole beneficiary of his IRA. They have two adult children, ages 35 and 25.

When	What Happens
During the IRA owner's life	Beginning at age 70½, the IRA owner takes his required minimum distributions (RMDs).
IRA owner dies at age 75	The surviving spouse rolls the IRA over into her name. She names her two adult children as joint beneficiaries of her single rollover account.
Surviving spouse reaches age 70½	At age 70½, the surviving spouse begins taking her RMDs.
Surviving spouse dies at age 80	The children inherit the IRA assets. Each child receives RMDs based on the single life expectancy of the oldest child. They may not mix the funds with other IRA assets.

Spousal Beneficiary and Separate Inherited IRAs

An IRA owner, age 68, makes his spouse, age 62, the sole beneficiary of his IRA. They have two adult children, ages 35 and 25.

When	What Happens
During the owner's life	Beginning at age 70½, the IRA owner takes his required minimum distributions (RMDs).
IRA owner dies at age 75	The surviving spouse splits the IRA assets into two separate IRA rollover accounts. She names each of her two adult children as the sole beneficiary of one account.
Surviving spouse reaches age 70½	At age 70½, the surviving spouse begins taking her RMDs.
Surviving spouse dies at age 80	Each child inherits a separate IRA. Because there are two separate accounts, each child receives RMDs based on his or her individual life expectancy. They may not mix the funds with other IRA assets.

Nonspousal Beneficiaries and Separate Inherited IRAs

An IRA owner, age 68, has two adult children, ages 35 and 25. He splits his IRA into two separate accounts and names each child as the sole beneficiary of one account.

When	What Happens
During the owner's life	Beginning at age 70½, the IRA owner takes his required minimum distributions (RMDs).
The owner dies at age 75	Each child inherits a separate IRA. Because there are two separate accounts, each child receives RMDs based on his or her individual life expectancy. They may not mix the funds with other IRA assets.

A married IRA owner may need to obtain his or her spouse's written consent before naming someone in place of (or in addition to) the spouse as the primary beneficiary of the IRA.

Post-Death Beneficiary Planning

The stretch IRA examples shown here illustrate situations in which the beneficiary planning takes place **prior** to the account owner's death. However, IRS regulations allow for a certain amount of **post-death** planning. From a pool of potential beneficiaries, those who will ultimately receive the assets must be identified by September 30 of the year following the owner's year of death. This time delay allows for the removal of a potential beneficiary either through a qualified disclaimer, a cash distribution, or by dividing the IRA into separate accounts. The life expectancies of those who remain as of September 30 are then used to determine the RMDs for the years after death.

Any separate accounts must generally be established by December 31 of the year following the year of the account owner's death.

Seek Professional Guidance

Setting up a stretch IRA requires careful consideration of a number of issues:

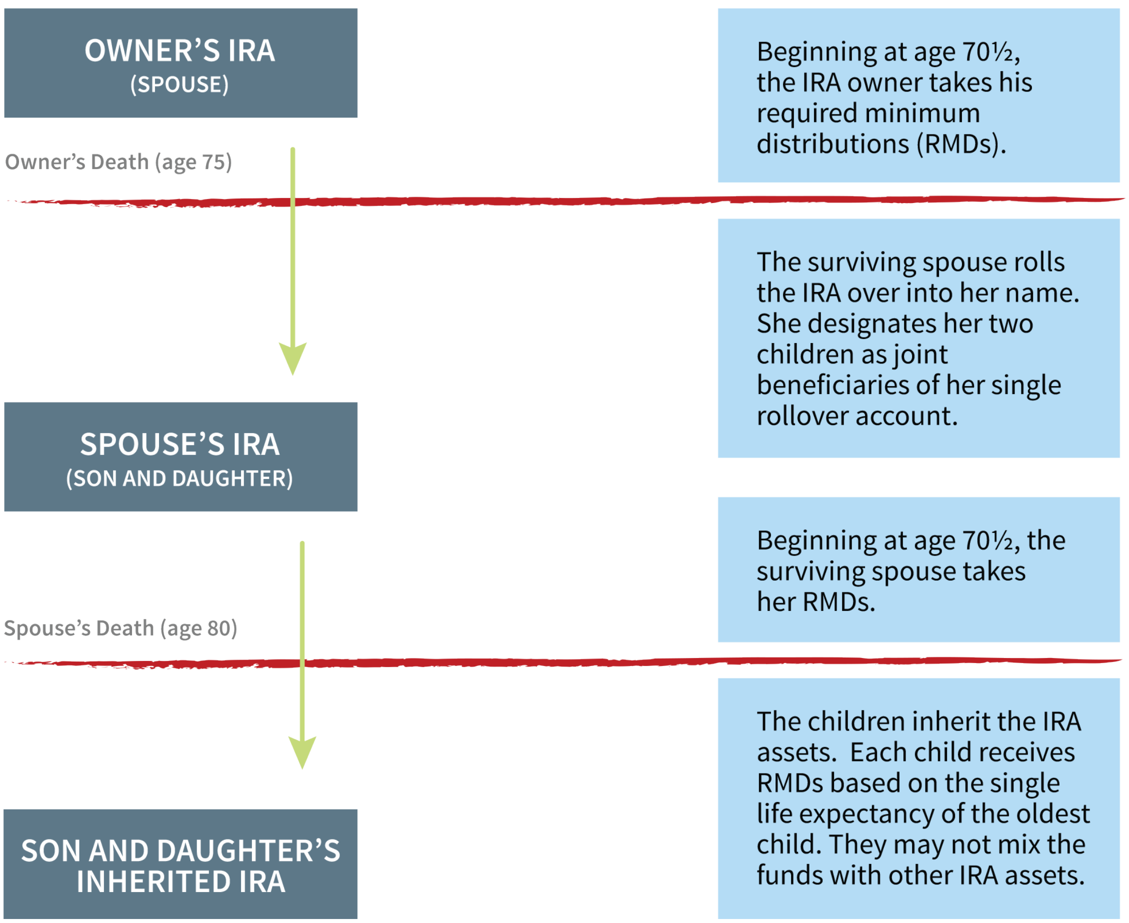
- Possible changes in tax law.
- The impact of inflation.
- The uncertainty of future investment results.
- The need to integrate the stretch IRA into the overall estate plan.
- The risks inherent in planning for an extended period into the future.

The guidance of appropriate tax, legal, and investment professionals is highly recommended.

How a Stretch IRA Works

Spousal Beneficiary and a Single Inherited IRA

An IRA owner, age 68, makes his spouse, age 62, the sole beneficiary of his IRA. They have two adult children, ages 35 and 25.

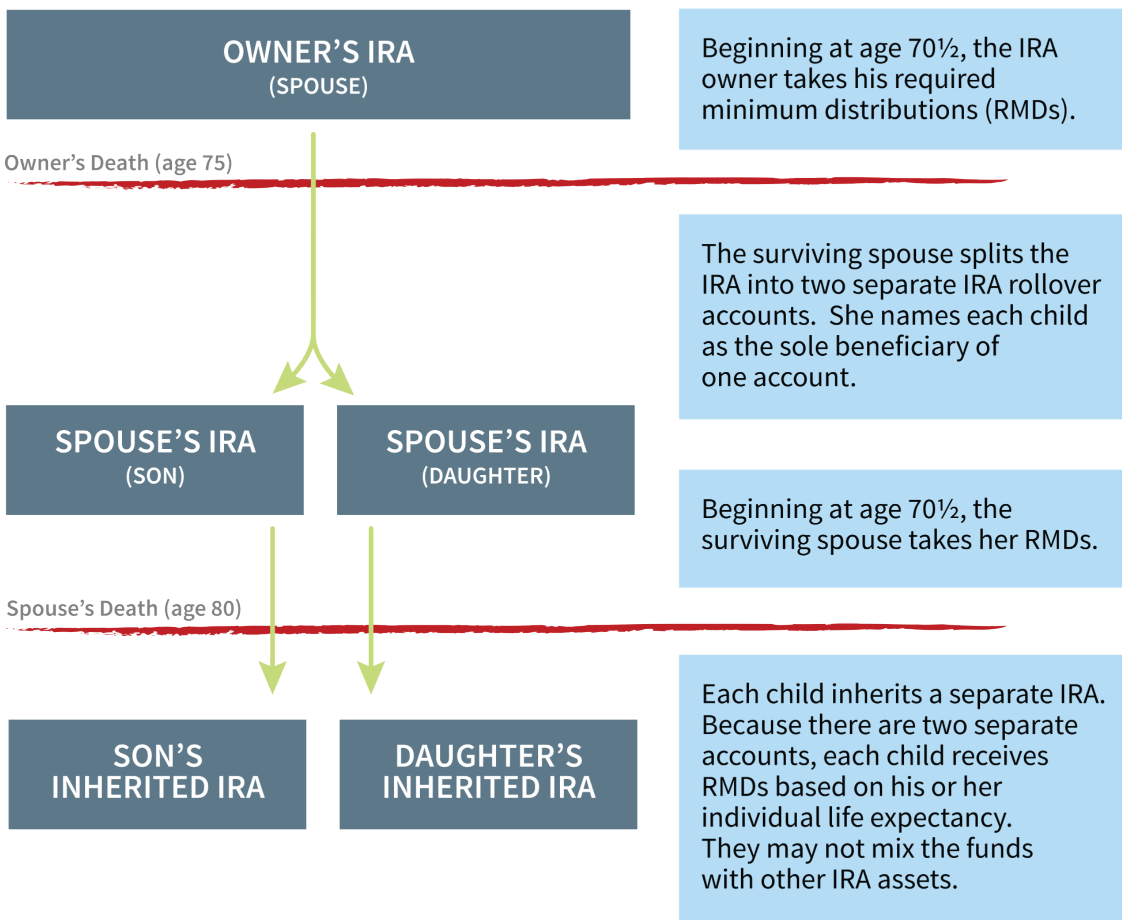


Note: This is one example of how a stretch IRA might be structured. Professional tax and legal guidance is strongly recommended.

How a Stretch IRA Works

Spousal Beneficiary and Separate Inherited IRAs

An IRA owner, age 68, makes his spouse, age 62, the sole beneficiary of his IRA. They have two adult children, ages 35 and 25.

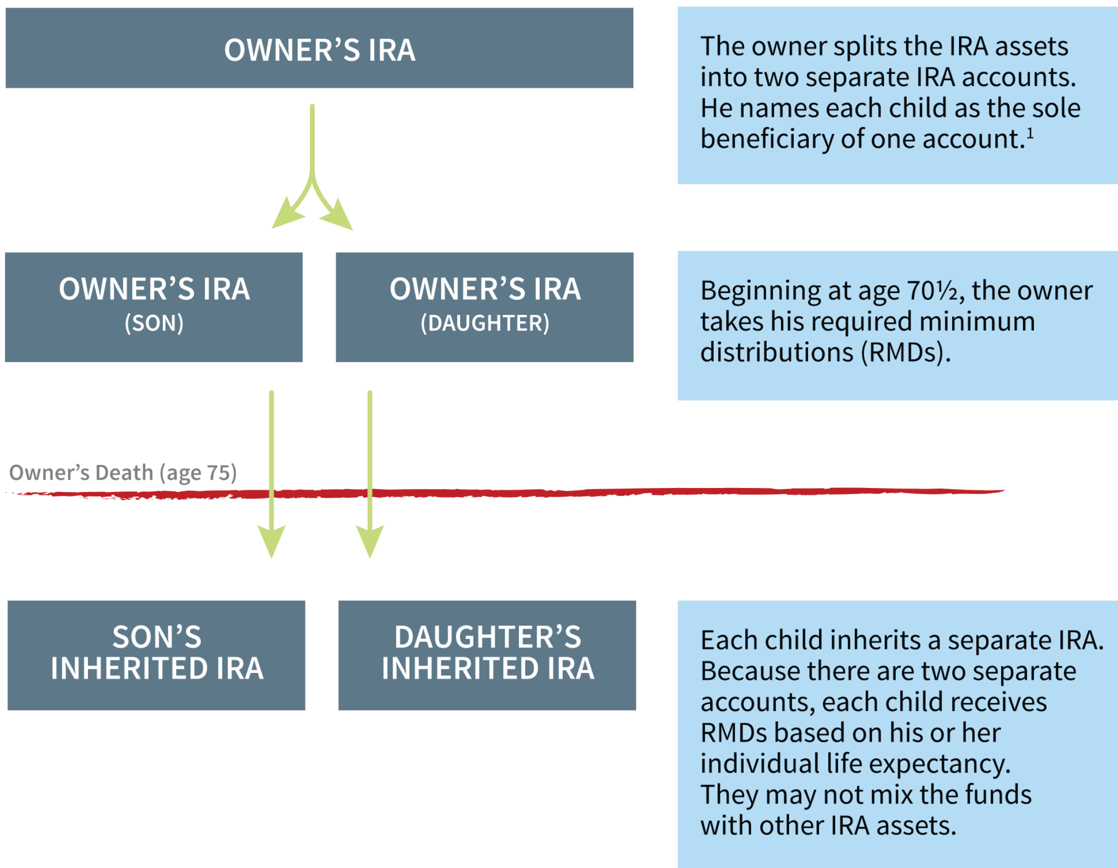


Note: This is one example of how a stretch IRA might be structured. Post-mortem distribution planning is also possible. Professional tax and legal guidance is strongly recommended.

How a Stretch IRA Works

Non-Spouse Beneficiaries and Separate Inherited IRAs

Assume an IRA owner, age 68, has two adult children, ages 35 and 25.



Note: This is one example of how a stretch IRA might be structured. Post-mortem distribution planning is also possible. Professional tax and legal guidance is strongly recommended.

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