

June 8, 2006

Gilligan and Mary Ann Smith
123 Sea View Road
Castaway Island, Pacific Ocean

RE: A 5 Step Action Plan for protecting your IRA's, 401(k's), and other Retirement Plans from Near Annihilation by the Taxman/THE RETIREMENT SAVINGS TIME BOMB . . . AND HOW TO DIFFUSE IT-America's IRA Expert, Ed Slott

Dear Gilligan and Mary Ann:

I appreciate the letter and information you sent to me relating to Gilligan's IRA, which is the primary asset in your marital estate. As I recall, this IRA currently is valued at over \$900,000. I appreciate and understand your concerns. You should be concerned that your planning is done properly and you should listen to the advisors you utilize.

I understand that your Dockside Life Insurance Agent is concerned about the manner in which we have structured your planning as it deals with the large IRA. I appreciate the opportunity to do my best to explain why I have planned and proposed what I have. I look at this as an opportunity to provide some answers to both you and your Dockside Life Agent. We have done some sophisticated planning here that is "out of the ordinary." Your trust has a significant amount of what I would call "specialized language" in order for it to work properly. As the article you sent me states, "if the trust fails to qualify as a designated beneficiary, then there is no designated beneficiary and the trust beneficiaries will not be able to stretch post-death required distributions even over the surviving spouse's life expectancy." This is a scary statement. Let me assure you that your trust is drafted with all of the proper provisions so this is not a concern.

You need to understand that your situation is not the normal planning situation. Therefore, it is difficult to take statements made by authors of articles and books to the public, at large, particularly "blanket statements" such as the one in the book you provided copies of, as it almost never appropriate for an author to make such a bold statement:

“there is no tax benefit that can be gained with a trust than without one.”

AND

“The only reason to name a trust as a beneficiary of your IRA is for personal (non-tax) reasons, such as restricting access to the build-up by beneficiaries who might be too young.”

In your situation, I find both of these statements to be false. Using Gilligan’s trust as the beneficiary of the IRA allows us flexibility in tax decisions that we simply don’t have without it.

Where should we start?

First of all, I want to review some of the facts that will impact the decision about how the benefits should flow upon Gilligan’s death.

1. Which spouse will die first?
2. How much of this IRA will remain intact or “qualified” at Gilligan’s death?
3. What will the value of your estate be at the death of the first spouse?
4. What will the value of your estate be at the death of the second spouse?
5. Will any of your children become incapacitated prior to the death of both of you?
6. What will Congress do with the Federal Estate Tax prior to the death of each of you?
7. What will happen with Kansas Estate Tax prior to the death of both of you?
8. Will any of your children develop taxable estates under federal or state law prior to your deaths?
9. How will the market perform between now and the death of the first spouse?

WHY WE WANT MAXIMUM FLEXIBILITY IN SPOUSAL PLANNING FOR LARGE IRA

The goal in the planning I have done for the two of you is to make sure that we have flexibility for the surviving spouse to wait and see what the best choice for the beneficiary of the IRA will be:

- a. all to spouse?
- b. part to spouse and part to children?
- c. all to children?

We want to be able to make the decision at a time when we know more answers than we do today.

The primary asset in your marital estate is Gilligan’s Qualified Retirement Plan funds (IRA). By having Gilligan’s trust be the beneficiary of the IRA it allows us to wait until his death occurs and at that time ask questions that may allow us to better control those benefits based on all of the “what if’s.”

First of all, the trust complies with all of the IRS and Federal Rules and Regulations that allow us to have this trust as a beneficiary. These are spelled out on page 243 of the book you provided to me:

- The trust must be valid under state law.
- The trust must be irrevocable at Gilligan's death.
- The beneficiaries of the trust must be identifiable.
- A copy of the trust instrument must be provided to the financial institution with the account by October 31 of the year following the year of the IRA owner's death.

Will Gilligan be the first to die? If, yes, here are the options:

First-what is the total value in both trusts or the entire marital estate? If it all goes to Mary Ann, will there be a potential estate tax concern at her death? Under current law, if congress makes no change to the existing law and Mary Ann lives past December 31 of 2006, all value in her estate over one million dollars is going to be subject to federal estate tax at a rate of 50%. Mary Ann has over \$300,000 of value in her trust, and that is likely to increase. If the entire IRA rolls over to her, then she will have a significant amount over one million dollars in value.

If we planned more traditionally, with Mary Ann as the primary beneficiary and your adult children as the contingent beneficiaries, the only option would be for her to disclaim all or a portion of the IRA to children.

What if we really wanted it all to be available for her benefit-just not all subject to estate tax? This is the flexibility of the trust. If Mary Ann disclaims an interest in all or part of the IRA under Article Seven of your trust, what happens? The portion disclaimed goes to the Family Trust (Credit Shelter trust) and is not rolled over to Mary Ann. Who are the beneficiaries of this trust? Your spouse and descendants. All income is to be distributed to Mary Ann annually as Mary Ann would be the oldest beneficiary. The required minimum distributions would be based upon her life expectancy.

Section 5.04 of Gilligan's trust tracks the regulations for IRA's which provide that you have until September 30th of the year following the year in which Gilligan's death occurs to make a determination as to who the oldest beneficiary is for the purpose of determining the amount of the required minimum distributions. If we really wanted these IRA benefits to go to children while Mary Ann is living, she can disclaim an interest in the Credit Shelter trust. This would make the children the beneficiaries of the IRA and the required minimum distributions would be made based upon the life expectancy of the oldest child.

What if we don't want to put the IRA or any portion of it in the Credit Shelter because the exemption equivalent for Federal Estate Tax exceeds the value of the total marital estate? Article Seven of Gilligan's trust provides all trust property is to be distributed outright to the surviving spouse unless disclaimed. We are where we want to

be without having to do anything. If this is the case and Mary Ann is competent, the IRA can simply be rolled over to her as a “spousal rollover” and we are where you would want to be. The children can be the designated beneficiaries and in the event of Mary Ann’s death, if she has made the IRA her own, the children can stretch out the benefits over their entire lifetimes.

This allows us some incredible flexibility to address tax concerns within the trust.

What if Mary Ann is the first to die? At Gilligan’s death, then the trust provides that all assets are to be distributed outright to your descendants (living children and descendants of any deceased children). Under the IRA regs relating to trusts, again, there are rules that allow a trust to operate as a “see through.”

The code allows retirement plan death benefits to be distributed in annual installments over the life expectancy of the participant’s Designated Beneficiary. **ALTHOUGH THE GENERAL RULE IS THAT A DESIGNATED BENEFICIARY MUST BE AN INDIVIDUAL**, the regulations allow you to name a trust as a beneficiary and still have a designated beneficiary for purposes of the minimum distribution rules. *If a plan participant dies leaving his retirement benefits to a trust that satisfies the four requirements of a valid trust, then, the beneficiaries of the trust (and not the trust itself) will be treated as having been designated as beneficiaries of the employee under the plan. . . Reg. Section 1.401(a)(9)-4,A-5(a).*

The IRS calls a trust that passes these rules a “see-through trust,” because the effect of passing the rules (for determining the beneficiary or beneficiaries) is that the IRS will look through, or see through, the trust, and treat the trust beneficiaries as the participant’s Designated Beneficiaries, just as if they had been named directly as beneficiaries of the retirement plan.

If you still have concerns, please let me know and lets get together to discuss it further.

Sincerely,

Tim J. Larson