The Benefits Of Using An Individual Retirement Account Trust

Individual Retirement Accounts (and other forms of retirement accounts) are now a major portion of many of my clients' assets. They were established to supplement social security and to fill the gap left by the loss of the pension plans that used to be more prevalent. In order to encourage more people to contribute to these accounts, the contributions to an IRA tax deductible and the growth within the accounts is tax deferred.

Since the accounts were designed to be used during retirement, there are also rules for "required minimum required distributions" after the IRA owner is 70½ based on the account holder's remaining life expectancy. If the IRA owner's spouse is the beneficiary, she can roll it over and set it up as her, taking the required distributions over her lifetime.

The tax-deferred growth of IRA's provide a great advantage for investment growth. However, IRA's often prove to be somewhat challenging to pass on to your children and even granchildren. The IRS has very specific rules about how to make sure your children are able to retain the advantages of tax-deferred growth of the IRA. If these rules are not followed exactly, the IRA may have to be liquidated over one to fine years and the tax deferral advantage that you want to pass on to your children is lost.

Even if all the rules are followed, there is no guarantee that your children will understand the long-term benefits of leaving the assets in the IRA and taking only the required minimum distributions. According to recent IRS statistics, more than **85%** of IRA balances are withdrawn by children beneficiaries within six months following the account holder's death. Not only does this result in a loss of the tax-deferred growth, there may be very little left of the money pulled out, after income taxes on the distribution are paid..

A IRA that is set up to allow beneficiaries to continue to enjoy this tax-deferred growth over their lifetime is often known as a "stretch" IRA. A "stretch" IRA creates enormous savings and potential tax deferred growth. One of my clients, Dorothy, had a relatively modest IRA of approximately $200,000 and named her 2 children as beneficiaries. Her son, Alan was forty three years old when he inherited his $100,000.00 share of the IRA.

If Alan just cashed in his share as the IRS report found is most common, he will realize approximately only $62,000 to $70,000, depending on his income tax rate,

Dorothy realized that even if Alan was wise enough to keep the IRA intact, Alan's wife was a spendthrift and would exert considerable pressure on him to cash it in for a new kitchen or fancy vacation. So Dorothy created and IRA Retirement Trust which mandated that Alan only withdraw his minimum required distribution each year. Extra amounts can only be withdrawn if there is a real need.

What is the difference for Alan if he withdraws no more than the minimum amount?

Each year he will take the required minimum distribution based on his age and life expectancy. In the first year after Dorothy's death, he would withdraw $1,870.00. This number is based on the IRS Uniform Life Table.

If we assume that over his lifetime, Alan's share of what is a quite modest IRA grows at an average rate of 7%, then over his lifetime he will be able to withdraw over $1.3 million from the IRA share that his mother left him. Dorothy would much rather leave Alan a net $1.3 million, than $70,000. Even if the average growth over Alan's lifetime is less than 6%, the advantages of tax-deferral still produce remarkable results.

Many of my clients have chosen to use an IRA Retirement Trust to ensure that their children or grandchildren will be able to benefit from the remarkable advantages that their IRA has provided to them. Grandchildren are often named as one or more of the beneficiaries of an IRA Retirement Trust.

Because of their younger age when they inherit, grandchildren can be ideal beneficiaries as they will realize many more years of "stretch out" growth. IRA Retirement Trusts are also used as an excellent way to help parents provide for an adult child who will have little or not retirement benefits when she retires. Finally, an IRA Retirement Trusts also provides protection to adult children beneficiaries in case of divorce or creditor problems.

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