

Expert Opinion Tax

**Planning under SECURE 2.0 for Beneficiary Designation to Trust for Spouse**

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I. Introduction

For married persons, this article addresses federal income and estate tax rules and planning techniques governing IRA beneficiary designations that name trusts as beneficiaries, focusing in particular on provisions for the surviving spouse in the context of credit shelter/marital deduction planning. These rules changed substantially in recent years, first by legislation known as “SECURE 1.0” in 2019, and then amended by “SECURE 2.0” in 2022, and by the final regulations issued in 2024 in Treas. Reg. § 1.401(a)(9). These rules are inordinately complex, affected by many different factual scenarios, the basic formats of which are reviewed below. Many similar planning issues and opportunities are presented in planning for employer-sponsored qualified retirements plans – notably, 401(k) plans and the like – but those plans often contain limitations on flexibility which may foreclose trust strategy options for beneficiary designations and generally are not discussed in this article.

IRA plans may be more, but not less, restrictive than Federal law permits. For the purposes of this article, IRA plans are assumed to provide their participants with the maximum tax flexibility allowed. As a note of caution, not all IRA providers have updated their forms to take into account SECURE provisions. For this reason, a careful review by practitioners of any forms needed to implement a proposed estate for a particular client, as well as plan summary materials, is prudent to permit the practitioner to alert clients of any potential issues to take up with their IRA provider.

Since this article is focused on credit shelter/marital deduction planning, the only eligible designated beneficiary (EDB) examined in this article is the IRA participant’s surviving spouse. Special rules that apply for beneficiaries who are disabled or chronically ill or less than 10 years younger than the participant are not addressed, and planning for minor beneficiary remaindermen

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<sup>†</sup> This article appeared in 2 parts, on September 11 and 21, 2026.

is addressed only to a limited extent. Also, planning is not addressed, except to a limited extent, for “Roth” IRA conversions and qualified charitable distributions. Federal generation-skipping transfer (“GST”) tax exemption issues are addressed only to a limited extent, because allocation of GST exemption to non-IRA assets is typically more advantageous.

## II. Beneficiary Designation Outright to Surviving Spouse

To explain the rules relevant to naming a trust for the benefit of a surviving spouse as an IRA beneficiary, it is necessary to briefly review the planning alternatives available when the surviving spouse is named individually as the beneficiary of an IRA account. Factors to consider are whether, at the death of the participant, the participant has already begun to take required minimum distributions (RMDs), and whether the surviving spouse has reached the age when he or she is required to take RMDs.

If the participant dies after his or her required beginning date (RBD), alternatives for the surviving spouse to consider as beneficiary and as not owner of the IRA are twofold. First, the surviving spouse has the choice generally available to EDBs to take RMDs over the greater of the surviving spouse’s life expectancy, in the case of a spouse recalculated annually using the Single Life Tables, or the participant’s life expectancy in the year of his or her death not recalculated (the “ghost life expectancy”). In addition, the surviving spouse has a special election (available only for spouses) to choose (sometimes called the “Section 327 election”) to have the inherited IRA be treated as if the surviving spouse were the employee. This would permit the Uniform Lifetime Table to be used, with life expectancy recalculated annually, and would stretch out the IRA distribution significantly, similar to the distribution period of a spousal IRA rollover. Under all of these options, the survivor is still treated as the beneficiary of the participant’s IRA and must begin taking RMDs the year following the participant’s death.

The spouse also may elect to be the owner of the account by rolling the account over, either to a new IRA account or to an existing IRA account of his or her own. These options permit the spouse to begin taking RMDs at the time of his or her RBD – age 75 for anyone born after 1959 (or earlier -- age 73 -- for persons born before then). Assets remaining in the IRA account at the surviving spouse’s death pass either to the contingent beneficiaries designated by the first spouse to die or to beneficiaries designated by the survivor, depending on the terms of the IRA plan (including its default provisions).

If the participant dies before his or her RBD, subject to limitations imposed in the plan document, the spouse, as an EDB, will be permitted to take RMDs over his or her life expectancy, recalculated annually using the Uniform Lifetime Table, and is not required to begin taking RMDs until the year in which the participant would have reached his or her RBD. At that time, the spouse may decide to elect instead to roll over the IRA into his or her own account.

Generally, the most attractive option for income tax purposes, whether the participant died before or after his or her RBD, is for the surviving spouse to roll over the decedent’s IRA account. Once the survivor reaches his or her RBD, the survivor begins taking RMDs over the longest applicable time period permitted. To determine this period, the surviving spouse’s life expectancy is determined under the Uniform Lifetime Table – the same table that would have

been applicable to the participant, had he or she been living – with the added benefit for a separate rollover account that the survivor's life expectancy is recalculated annually. The effect of recalculation of life expectancy each year is twofold: (i) this extended RMD period cannot exhaust the IRA account during the survivor's lifetime unless the spouse lives beyond the last age (age 120) specified in the Uniform Lifetime Tables; and (ii) the size of the RMD is recalculated annually by dividing the value of the IRA account by the surviving spouse's life expectancy each year. At the survivor's death, the remaining IRA account assets pass to the beneficiaries designated by the survivor.

A distinction between inherited IRAs and rollover IRAs is the period required to be used to receive RMDs by the beneficiaries of the account after the death of the surviving spouse. For the spousal inherited IRA, upon the death of the surviving spouse, distributions will be made, starting with the year following the spouse's death, over the spouse's remaining life expectancy (not recalculated), with the last payment to be made on the earlier of 10 years after the spouse's date of death or the end of the spouse's life expectancy. Only if an EDB is designated as a beneficiary can the stretch-out exceed 10 years (e.g., for a minor child until age 31). For the spousal rollover IRA where descendants are the designated beneficiaries and none of them are an EDB, the 10-year rule generally applies and annual RMDs (based on designated beneficiary life expectancy) must be made, with the remaining IRA balance distributed at the 10<sup>th</sup> anniversary of the spouse's death.

Two important additional items to note relate to Roth conversions and qualified charitable distributions (QCD). First, while a Roth conversion is available to the surviving spouse for a rollover IRA, a Roth conversion is not available for a spousal inherited IRA (unless the spouse makes the special Section 327 election to treat the IRA as his or her own). Second, a QCD for a rollover IRA or an inherited IRA may be made any year after the surviving spouse attains 70 ½ years of age. The distribution (which counts for RMD purposes) must be made by the IRA plan administrator directly to a qualified Section 501(c) (3) charity and in 2026 is limited to \$111,000.

Even in situations where a rollover IRA would be more advantageous from an income tax perspective, other factors may point to a different choice. This may occur in the case of a relatively small IRA account which is expected to be paid out in the nearer term after death of the first spouse. Even in the case of a larger IRA, practical difficulties (for example, where the survivor's capacity is diminished) may impede effecting a rollover. In such cases, an IRA beneficiary designation into a conduit trust for the survivor, as discussed below, may be a better planning option.

### III. Beneficiary Designation in Trust for Surviving Spouse

For a beneficiary designation to a trust for the surviving spouse, different rules apply depending on whether the death of the first spouse occurs before or after his or her RBD, whether the trust is structured as a conduit trust or an accumulation trust and whether the trust is intended to qualify for the marital deduction for federal estate tax purposes.

Also important, for a Section 401(k) plan or other non-IRA type of qualified retirement account, is whether the plan permits the same stretch-out opportunity available for an IRA. Where there

is a limitation under the plan, consideration should be given, where viable, to make a rollover distribution to the participant's own IRA. The remaining stretch-out period after the survivor's death is also relevant.

Regardless of whether the participant dies before or after his or her RDB, a QCD distribution is not available for either a conduit trust or an accumulation trust. Likewise, a Roth conversion is not available for an IRA held by a conduit trust or accumulation trust.

A. Death after RDB.

Different tax income treatment depends on whether a conduit trust or an accumulation trust is designated as beneficiary.

1. Conduit trust. A conduit trust requires that all RMDs received by the trust be distributed directly to the beneficiary of the trust. Because the surviving spouse is entitled to receive the RMD annually, the survivor is considered to be the EDB. As a result, the spouse may elect the same maximum available stretch-out period under the Uniform Lifetime Table, with annual recalculation, as is available for an IRA rollover. This election became available under Secure 2.0, which has extended the stretch-out period beyond the shorter period (limited to the surviving spouse's life expectancy under the Single Life Table) previously available under Secure 1.0. This can be an attractive option in a second marriage where each spouse wishes to benefit his or her own children at the survivor's death. However, the surviving spouse as the beneficiary of the conduit trust may elect instead to use the Single Life Table and receive larger minimum distributions. For the participant who wishes to prohibit this result, the participant may notify the plan administrator and foreclose the election-out of the Uniform Lifetime Table by the spouse. For example, the difference between the required minimum distributions for a 75 year old using the Single Life Table (Secure 1.0) and the Uniform Lifetime Table (Secure 2.0) is substantial: for a \$3,000,000 inherited IRA the RMD under the Uniform Lifetime Table would be \$121,951 (roughly 4.05% of the IRA) while the RMD under the Single Life Table would be \$202,703 (roughly 6.75% of the IRA). Additionally, under certain circumstances an even shorter period might be available under the participant's ghost life expectancy or the "at least as rapidly" rules.

One drawback in the use of a conduit trust is that RMDs must commence the year after the participant's death and cannot be deferred until the survivor reaches his or her own RDB, as may be done in the case with an IRA roll-over. If the survivor has reached his or her RDB at the death of the participant, the IRA rollover will yield approximately the same result as the conduit trust in the stretch-out period and typically will yield no meaningful difference if the survivor is close to his or her RDB. The Treasury Regulations specify that the survivor cannot elect the short 10 year period if the participant has died after his or her RDB.

For the stretch-out period at survivor's death, rules similar to a spousal roll-over apply. Where the beneficiaries upon the survivor's death are descendants, none of whom is an EDB, for remaining distribution the beneficiaries must receive distributions calculated on the remaining life expectancy of the survivor without recalculation starting the year after the survivor's death,

and the remaining IRA account assets must be distributed at the 10<sup>th</sup> anniversary of the survivor's death.

2. Accumulation trust. An accumulation trust is a trust that is not required to distribute RMDs to its beneficiaries. Where the survivor is not entitled to receive the RMDs, then the survivor is not considered to be an EDB. Secure 1.0 imposed a 10-year maximum stretch-out period for an accumulation trust for the surviving spouse. If the trust is a fully discretionary trust – meaning that no distribution is required to be made to the survivor – then the trustee is in full control of the level of distributions to the survivor, and whatever remains at the survivor's death passes to the trust remainder beneficiaries. Importantly, the 10-year rule stretch-out period may be reduced to a shorter period if the trust property may pass to a charitable organization at the survivor's death – the longer of 5 years or the remaining “ghost life” of the first spouse to die. Also, the annual RMDs must be calculated based on the survivor's life expectancy, under the Single Life Table, without recalculation, over a 10 year period commencing at the participant's death, after which time the entire remaining IRA assets must be distributed to the trust.

If the survivor dies before the end of the 10 year period, then the remaining RMDs must be made using the deceased surviving spouse's single life expectancy over the remainder of the 10 year period.

3. Marital deduction/ credit shelter trust. A conduit trust will qualify for marital deduction treatment if the trust also contains a provision that requires the IRA net income, if greater than the annual RMD, be distributed to the surviving spouse. The same requirement can be included in an accumulation trust to qualify for the marital deduction. Typically, this provision is included in a marital deduction trust where the IRA assets are not needed to be utilized in a credit shelter trust for estate tax planning purposes. For some spouses, however, IRA assets must be used for credit shelter trust planning – as often is the case for residents of New York, which has an estate tax exemption (\$7,350,000 in 2026) lower than the federal exemption (\$15,000,000 in 2026) and does not allow portability of NY exemption to the survivor. For those situations, an accumulation trust can be a better option, given the flexibility to retain net income in the trust, with distributions only to the survivor if needed. In general, traditional IRA accounts are considered to be a less advantageous asset for use in a credit shelter trust because of their embedded income tax burden and are used only when no other assets are available.

A separate relevant concern from an income tax perspective is that, where an accumulation trust contains other assets, the income tax character of any distribution to the survivor will depend on the overall trust income under pro rata rules for distributable net income (DNI) purposes. If only RMDs are taken for the first nine years, distribution of the balance of the IRA account in the 10<sup>th</sup> year may cause a disproportionate amount of ordinary income from the IRA to pass as DNI as part of any trust distribution to the spouse in that year. Of course, retaining any IRA distributions in the trust will likely subject the income to higher income tax rates under the compressed trust tax rates. Accordingly, some significant distribution from the trust to the spouse in the 10<sup>th</sup> year should be considered for some situations, with a view toward overall income tax minimization between the trust and the spouse.

Two special items to note relate to Clayton trust planning (a flexible estate planning provision that permits the decedent's estate to determine how assets are allocated between the marital and non-marital trusts) and taker of last resort provisions (generally applicable where no family member is living, either at the participant's death or at the trust termination). For Clayton provisions where conduit trust treatment is desired for the entire IRA account regardless of the extent to which the Clayton election may be made, it is important that the provisions requiring distribution of the net income of the IRA, if greater than the RMD, to the trust and then to the surviving spouse be included in both the marital trust and credit shelter trust. As to takers of last resort, a contingent disposition to charity for an accumulation trust is a trap for the unwary, as this may require, commencing at the participant's death, that the longer of a 5-year stretch-out period or ghost life expectancy (but not to exceed the 10-year distribution period to the trust for the spouse), is applicable when participant dies after his or her RBD during the survivor's lifetime. If the trust remainder is to continue in trust for descendants, that potential negative treatment may be able to be avoided via a marital trust, or a credit shelter trust in which the spouse is the only beneficiary during his or her lifetime. This is because a new class of so-called "countable beneficiaries" is specified in the trust instrument to receive the trust property upon the spouse's death – thereby supporting the position that the more remote contingent charitable disposition should not be recognized to "count" for 10-year rule availability purposes. On the other hand, a credit shelter trust in which the spouse and descendants are all discretionary beneficiaries, with remainder (either outright or in trust) for descendants, is more problematic, because no new class of beneficiaries is created upon the spouse's death.

GST tax planning is typically not a concern for IRA accounts held in a marital trust, where GST exemption (if needed) may be allocated at the survivor's death. For a credit shelter trust, however, GST exemption allocation issues should be considered as part of the participant's estate planning for any trust property which may pass for grandchildren (either at the survivor's death, or later).

#### B. Death before RBD.

The income tax treatment depends on whether a conduit trust or an accumulation trust is designated as beneficiary. In particular, there is an important significant additional concern with a conduit trust if the participant dies before the participant's RBD.

1. Conduit trust. When the IRA participant dies before his or her RBD, RMD distributions may be deferred until the participant's RBD. Similarly, when distributions commence, the minimum distributions are computed over the surviving spouse's lifetime using the Uniform Lifetime Table, and the participant may foreclose use of the shorter Single Life Table. Although distributions to a surviving spouse who is the sole beneficiary of a conduit trust are generally computed using the spouse's life expectancy, the Treasury Regulations permit an IRA Plan Administrator to mandate the 10-year rule on all or some classes of EDBs (such as a spouse), or may permit the participant to elect it, or may permit the beneficiary to elect the 10-year rule. If the IRA plan is not limited to 10 years (important for the practitioner to check), it is unclear from the Regulations whether a surviving spouse who is the sole beneficiary of a conduit trust may elect this 10-year rule, or whether the election is to be made by the trustee. That may limit the utility of the conduit trust option for a participant who is looking for the maximum

stretch-out in order to preserve funds for the remainder beneficiaries, because the survivor may be able to withdraw the entire IRA assets from the trust upon the expiration of the 10-year rule period.

For the participant who is concerned that the spouse might elect the 10-year rule, an accumulation trust might be selected instead. However, an alternative might be to select a conduit trust, but also to include in the trust instrument a provision that the trustee, in the exercise of trustee discretion, may convert it to an accumulation trust before the beneficiary finalization date (BFD) -- that is, September 30 of the year after the participant's death. This would allow the trustee to have a meaningful period of time after the participant's death to secure a waiver from the spouse, thereby ensuring that the Uniform Lifetime Table will govern the RMDs. If the spouse is unwilling to provide a waiver (or, if it is discovered after the participant's death that the IRA plan only allows 10-year rule treatment), the trustee could convert to an accumulation trust. For this option to be practically viable from a fiduciary standpoint, guidance to the trustee from the participant is important -- either in the trust instrument or a separate letter of wishes -- along with exoneration of liability provision in the trust instrument. It should be noted that this structure might be reversed. In other words, an accumulation trust might be specified, with the flexibility in the trustee, in the trustee's discretion, to decide -- after a spousal waiver -- to convert to a conduit trust before the BFD. This structure may be more palatable from the viewpoint of the spouse -- that is, for the trustee to grant stretch-out tax treatment consistent with the participant's wishes if she cooperates and executes a waiver (rather than to take something away, if she does not).

After the survivor's death, the remaining stretch-out period is the same as described above where the participant dies after RBD.

2. Accumulation trust. During the survivor's lifetime, the treatment for an accumulation trust is largely the same as if the participant had reached his or her RBD, except that the participant's ghost life expectancy is not available if the participant has not reached his or her RBD at death. Likewise, the stretch-out period after survivor's death is the same as described above where the participant dies after RBD.

3. Marital deduction/ Credit shelter trust. Regardless whether the participant dies before or after his or her RBD, the considerations for marital deduction/credit shelter treatment are in general the same. From an estate tax planning perspective where the goal is to pass more to a future generation, one important practical difference is that designation of a credit shelter trust as the beneficiary may be even less desirable (assuming other assets are available instead) for a younger participant (whose spouse may likewise be younger), as actuarially the likelihood that a longer period of RMDs may more substantially deplete the trust principal.

#### IV. Conclusion

A broad range of factors and estate planning goals must be considered in making an IRA beneficiary designation for a surviving spouse. Particularly in a second marriage, trust designation can be attractive, often without significant loss of the long-term stretch-out available for an outright IRA rollover. In crafting the beneficiary designation planning, the practitioner

must carefully consider a number of technical issues (including, among other issues, special concern regarding the 10-year rule where the first to die has not yet reached his or her RBD) in order to carry out the spouses' objectives.

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