

Investment Insight: Naming Beneficiaries of Insurance Policies & Retirement Plans



Backert-Walker Financial Group of Hilliard Lyons

TONY BACKERT
Financial Consultant

WILLIAM S. FULLER
Financial Consultant

BRADLEY WALKER
Financial Consultant

10200 Forest Green Blvd
Suite 500
Louisville, KY 40223
502.426.0790
800.230.0790
TBackert@hilliard.com
www.hilliardfc.com/backertwalker

A major issue in estate planning is who to name as beneficiaries on life insurance policies, pension plan accounts, and IRAs. Naming beneficiaries can be complicated and can present estate and income tax consequences.

When naming beneficiaries, consider:

- **The beneficiary's age** — Many policies and plans will not directly transfer assets to minors until a trustee or guardian is approved by a court.
- **The ability of the beneficiary to manage the bequest** — Perhaps a trust set up in the person's name would be better than a direct transfer.
- **Rules pertaining to pension plans** — Unless waived by the spouse in writing, the law requires a spouse to be the primary beneficiary of the account.
- **Naming contingent beneficiaries** — Should something happen to your primary beneficiary, the contingent beneficiary would receive your assets.

PENSION PLANS AND INDIVIDUAL RETIREMENT ACCOUNTS (IRAS)

The law requires that a spouse be the primary beneficiary of a 401(k) or a profit-sharing account unless he/she waives that right in writing. A waiver may make sense in a second marriage — if a new spouse is already financially set or if children from a first marriage are more likely to need the money. Single people can name whomever they choose.

When retirement plan assets are left intact within an estate, spousal beneficiaries may inherit the money without paying federal estate or income taxes. After age 70½, the surviving spouse must begin required minimum distributions (RMDs) based on his or her life expectancy. The RMDs are taxed as ordinary income. This withdrawal schedule typically is preferable to cashing out the entire bequest at once, which is likely to trigger higher tax payments.

Investment Insight: Naming Beneficiaries

The complexities of building, preserving and passing along wealth have never been greater. Investors are increasingly seeking guidance and comprehensive solutions that consider their unique circumstances and long-term goals. It's my pleasure to work with such individuals to offer insight, advice and solutions in helping them reach their goals.

With an IRA, spousal beneficiaries may transfer assets to an existing IRA and designate themselves as the account owner. These transfers typically do not trigger tax payments as long as a spouse follows rules for trustee-to-trustee transfers. After age 70½, a spousal beneficiary is mandated to take annual RMDs, which are based on the surviving spouse's life expectancy and are taxed as ordinary income.

Nonspousal beneficiaries have two options when inheriting an IRA: They may take all distributions within five years of the original account owner's death (if decedent wasn't subject to RMDs) or take annual distributions determined by the life expectancy of either the beneficiary or the decedent, whichever is longer.

LIFE INSURANCE

No matter who is designated beneficiary of a life insurance policy, the death benefit proceeds are income tax free. Unlike property disposed of in a will, if the beneficiary designation form is properly completed, insurance proceeds do not go through probate.

For many married individuals, a spouse will be the most logical beneficiary. A trust may be a prudent beneficiary choice, however, if a surviving spouse would not have the ability to prudently manage a large sum of money. The trustees (often a legal entity rather than an individual) would then take charge of managing, investing, and disbursing the policy proceeds for the benefit of the surviving spouse.

KEEP YOUR PLAN UP-TO-DATE

Should you change your estate plan or will, it is imperative to readjust all beneficiary designations so that your estate plan accurately reflects your desires.

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