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## Costly Errors Relating to Beneficiary Designations for IRAs & Qualified Plans

An IRA or qualified plan is often a family's largest investment. Improperly designating your beneficiaries, failing to name beneficiaries, or failing to update your designations, can have unforeseen and even disastrous results. A retirement plan that defaults to the estate is subject to debts, taxes and creditor claims, in addition to accelerated income tax. What follows are the most common mistakes and some simple solutions.

**1. Losing the beneficiary designation form.** The form controls. Banks and financial institutions frequently merge, get sold or move and the files are lost or misplaced. Do not assume that the plan administrator will have your form when you die. Without it, your loved ones are at the mercy of the default provisions of the plan. The solution is to keep your own records. Ask for a copy of the acknowledged beneficiary form from your plan administrator and keep it with your other estate planning documents.

**2. The form is out of date. Have there been changes in your life?** All too often, people forget to update their beneficiary forms. For example, Bob and Jane were married in 1981 while Bob was an employee of a corporation and a participant in its qualified retirement plan. Bob designated Jane as his beneficiary. When Bob and Jane divorced in 2004, her rights to Bob's retirement benefits terminated under the Decree. Bob never changed his beneficiary form. When he died in 2011, the plan administrator disbursed the funds to Jane, in reliance on Bob's beneficiary designation form! The solution is to review the form annually at the same time each year, a birthday, anniversary or even at tax time when you review your financial records anyway.

**3. No "backup" beneficiary.** You can designate both primary and secondary or contingent beneficiaries. A primary beneficiary receives the proceeds of your account at your death. A contingent beneficiary is an alternate person, organization/entity, trust or estate who receives all or a portion of your account if none of your primary beneficiaries survive you. It is important to note that your contingent beneficiary only receives the proceeds of your account if you have no surviving primary beneficiaries at the time of your death. If you fail to designate a beneficiary or if all of your primary and contingent beneficiaries predecease you, the rules of the financial institution or plan that administers your account usually contain a default provision which will govern how your account gets distributed. This default provision may be contrary to your wishes.

**4. Misunderstanding the designation.** Unless you understand the form, it is possible to accidentally disinherit a loved one. For example, if you name your three children as primary beneficiaries, intending each child to receive one-third, and your oldest child predeceases you, at your death your two surviving children will each receive one-half. Your oldest child's family gets nothing.

Similarly, if you list your daughter, the mother of your grandchild, as the 50% beneficiary on your account and your two bachelor sons as 25% beneficiaries and your daughter predeceases you, each son would absorb half of your deceased daughter's share and receive 50% of the assets in the account. Your grandchild would inherit nothing. The solution is to ask questions of your plan administrator.

**5. Naming a minor child as a beneficiary.** A minor cannot control funds. There are at least two problems with designating a minor as the beneficiary of your retirement account: first, at your death a Guardian will have to be appointed by the Court to manage the assets for the child, and secondly, once the child turns 18, the assets are released into the hands of the child. The solution is to establish a Trust so the funds can be managed in accordance with your instructions by a responsible trustee of your choosing.

**6. Missing out on the Opportunity to S-T-R-E-T-C-H your IRA.** Stretching an IRA means allowing the account to grow, tax deferred, over the lifetime of the beneficiary. Statistics prove that this is a real money-maker. For instance, if a 30 year old beneficiary of a \$100,000 IRA account takes only the required minimum distributions and the funds earn an average of 7% over the life of the beneficiary, which IRS tables estimate at 53 years, the value of the account will grow to \$1,026,533! Naming a younger beneficiary can have even more dramatic results. Why doesn't this happen all the time?

Because almost 90% of IRAs are cashed out within 6 months of the death of the initial account owner. The solution may be to establish a trust to preserve the "Stretch Opportunity."

With correct planning, your retirement plan can preserve funds for future generations to enjoy. The planning starts with the beneficiary forms. It is important to understand that your Will does not control who gets your IRA. The beneficiary designation trumps your Will. Filling out the beneficiary designation form correctly is critical. At Berwitz & DiTata LLP we assist our clients in understanding their beneficiary designations and, if requested, assist them in completing the forms. We also remind our clients to review the forms periodically, and suggest that they place copies of the forms in their estate planning binders so that they can be easily located when needed.