https://www.unionleader.com/news/business/money_sense/money-ense-traditional-iras-and-the-implications-of-beneficiary-designations/article_d1ca1c92-cf8c-5f23-8b48-cae24d51fa5d.html

# Money$ense: Traditional IRAs and the implications of beneficiary designations

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WHEN YOU completed your Traditional IRA application, you probably filled in a beneficiary designation form as part of the process. This is the form that indicates who will receive the balance in the account at your death. This column will discuss Traditional IRAs — not Roth IRAs or employer-sponsored retirement plans; they have some of their own rules!


It seems straightforward enough, but your choice of beneficiary can have consequences for other areas of your or your heir's financial life. Among them are the size of the required minimum distributions (RMDs) and how fast your heirs must take the funds from the account at your death.

Though federal tax law may require the surviving spouse to have rights to certain retirement-plan assets, traditional IRAs aren't affected by this. The impact might come from state tax laws that impose requirements on IRA beneficiaries. This might be true if you live in a community property state. The state law might give your spouse legal rights to your IRA even if he or she wasn't named as a beneficiary. It is important to discuss this with an estate planning attorney with knowledge of your state law.

An area that federal law does affect is required minimum distributions. Once you reach age 70½, you must begin to take money from your IRA. This needs to happen by April 1 of the calendar year following the calendar year in which you turn age 70½.

There is a specific formula used to calculate the amount that you need to withdraw. It is based on the account value and a life expectancy table. Your beneficiary choice usually doesn't affect the results. One important exception to this does exist. If your spouse is your sole designated beneficiary for the year you are taking the funds and he or she is more than 10 years younger, then you will need to use a different life expectancy table for the calculation.

At your death, the beneficiaries you named will receive the funds. Usually distributions must begin by the end of the year following the year of death. If you haven't yet taken any of your own RMD in the year you die, your beneficiaries must take this withdrawal.

Different types of beneficiaries have different withdrawal rules. This becomes important to review, since the longer that a beneficiary can leave the money in the IRA, the more time they can benefit from a tax deferral and spread out the tax liability over the years. An individual who is the designated beneficiary can usually use his or her life expectancy when calculating distribution amounts. A surviving spouse can generally use his or hers as well, but a spouse has other choices, such as the ability to roll the funds to their own IRA. Trusts, charities or even naming your own estate as beneficiary all have distribution implications.

Keeping track of your RMDs and making sure you take the correct amount is important. The penalty for failure to do so is 50 percent of the amount you should have taken, but didn't. This is on top of the income taxes you pay.

When choosing your beneficiary, be sure to name both a primary and contingent. The primary beneficiary will receive the funds first once you die. If your primary has predeceased you or declines to take the money, then your contingent beneficiary will receive the account. Who you designate as beneficiaries should be reviewed periodically. As life changes, your beneficiaries may change as well.

As this can be a complicated area of law, you should carefully consider your choices. Understanding the implications of these choices is critical. A qualified professional such as an estate planning attorney or certified financial planner can help you sort through the options and reach the best choice for you.

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