

IRA Update "Default" Provisions Can Determine Beneficiaries, Life Expectancies

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Practice Area: Estate Planning

Owners of Individual Retirement Accounts should periodically review their IRAs, paying particular attention to the "default" provisions that control payment of benefits if no specific provision has been selected. Default provisions determine beneficiaries. They also determine how life expectancies will be calculated.

Children as Beneficiaries

Unmarried individuals with children, who wish their children to be able to defer income tax on IRA payments received after their parent's death, should not name their estate as beneficiary of their IRA(s). Instead, they should name their children as beneficiary.

If the IRA owner names the estate and dies before age 70-1/2, all benefits will have to be paid within five years of his or her death. If the children are named beneficiary, and separate shares are created for each, they may instead receive distributions based on their respective life expectancies.

Income on the unpaid balance of their shares will accumulate free of income taxes until time of payment.

If a designated child predeceases an IRA owner, his or her share may pass to other children of the IRA owner, rather than the child's children or, under some IRA "default" provisions, to the child's spouse. If the share is to pass to the deceased child's children, this should be specifically stated.

Life Expectancies

Individual Retirement Account distributions are made over a period of time calculated to equal the life expectancy of the IRA owner and, if so elected, his or her spouse. This is done in two ways by electing either "recalculation" or "term certain."

With recalculation, life expectancies increase slightly each year, stretching the duration of distributions before death occurs. In the year following the IRA owner's or spouse's death, however, his or her recalculated life expectancy reduces to zero, shortening or ending the duration of distributions.

With a "term certain" election, life expectancy tables are consulted only once and the expected ages of the IRA owner and beneficiary never change. Life expectancies do not reduce to zero the year after death, often resulting in a longer span. (Those wishing to use a "term certain" should verify that their IRA contract permits it. The default provisions of many banks, insurance companies, and brokerage firms provide that a "term certain" life expectancy must be affirmatively elected in writing. If the agreement is silent, IRS regulations mandate recalculation.)

If the beneficiary is the owner's spouse, some couples choose to recalculate the owner's life expectancy but not the spouse's. This often produces a "best of both worlds" result. If the owner dies first, the spouse may roll over the IRA to a spousal IRA and continue to receive payments. If the spouse dies first, the owner will continue to receive payments for the balance of the owner's recalculated life expectancy.

It makes good sense to review the default provisions of all IRA agreements, electing different provisions when appropriate.

Your Estate Plan

The Wisconsin legislature has authorized a procedure that may be of interest to you.

It is now possible to bequeath items of tangible personal property via a written list rather than your will. At death, the property described in the list will be distributed to the named distributees as effectively as if the bequests were described in your will.

The list must be signed and dated by you. (Initially, it is also necessary to sign a codicil to your will referencing the list.)

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