

Surviving Spouse Can Take Steps to Maximize IRA Benefits

Apr 05 1996

Practice Area: Estate Planning

In a marriage, one spouse usually names the other as the preferable death beneficiary of his or her Individual Retirement Account.

The IRA provides cash for the surviving spouse's support. These payments, made directly to a spouse or to certain trusts, qualify for the federal estate tax marital deduction. Income taxes are payable only as distributions are received.

There are a number of practical steps the surviving spouse can take to maximize income tax deferral.

The surviving spouse may elect to treat the IRA as his or her own, divide it into separate accounts, and name each child a death beneficiary of an account. This permits use of a new joint life expectancy to determine the periodic payout.

A recent IRS letter ruling clarifies the tax results of this action. The ruling concerns a surviving spouse with three adult children. The deceased spouse had reached age 70-1/2 and had been receiving annual distributions from the four IRAs he owned.

(Distributions must begin when an IRA owner reaches age 70-1/2 and must equal certain minimum amounts. In order to collect the income tax that has been deferred, Congress wants distributions to be paid out over the lifetime of the owner and/or the spouse.)

The surviving spouse, who was also over age 70-1/2, combined the four IRAs into one and treated them as her own. (She might also have rolled them over into a new IRA in her name.) She then divided the IRA into three separate accounts, naming each adult child the death beneficiary of one account.

Had she maintained a single IRA naming all three as death beneficiaries, the life expectancy of the oldest child combined with her life expectancy would have determined the payout period. The use of separate accounts extended the duration of payouts for the other two accounts - further deferring income taxes.

The IRS ruled that the surviving spouse could elect to treat the IRAs as her own, even though she was over age 70-1/2. It further ruled that she could subdivide the IRA into three separate accounts, establishing a separate minimum required distribution for each.

Joint life expectancy is calculated one way when the parent is alive and another way after death. When the parent is alive, IRS regulations calculate the child's age as no more than ten years younger than the parent. After the parent's death, the actual life expectancy of the child governs the payout.

Creating a separate IRA for each child helps level the playing field after the death of the surviving parent. This approach also works if the spouse who sets up the IRA dies before age 70-1/2.

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