Financial Planning
Newsletter

October 2007

Newsletter Archives

CHOOSING YOUR IRA BENEFICIARY, IT'S MORE THAN A NAME

What's in a name?

Well, if it's the name of your IRA beneficiary, it can be more than you think. Properly naming IRA beneficiaries is one of the most important, yet often overlooked, estate planning moves a person can make. If you don't choose a beneficiary, your probate judge will and your account may not be distributed as you had intended. If a beneficiary isn't named, the IRA goes to the estate and the distribution is based on your will or by state law if you die without a will. There are several reasons why your estate is the worst place for the IRA to end up.

Estate as Beneficiary

If the IRA beneficiary is your estate, your account becomes subject to probate; the legal process of administrating and distributing one's estate. As part of the estate, the IRA is subjected to the claims of your creditors. Probate can be time consuming and costly; delaying and eroding the value of the asset for the final recipient.

Additionally, with your estate as beneficiary, a valuable opportunity to stretch the IRA over a longer period of time is lost for your final recipients.

Let's go though the distribution rules if the estate is the beneficiary of the IRA. If the owner dies before starting their required minimum distributions (RMD) at age 70 1/2, the final recipient will need to withdraw all assets from the IRA by the end of the fifth year following the year of the owner's death. If the owner dies after starting their RMD, the recipient must take withdrawals based on the deceased owner's life expectancy.

Individual as Beneficiary

Now if your beneficiary is an individual, they can stretch distributions over a potentially longer period of time to maximize the account's tax-deferred growth.

A spouse can roll over the balance to their own IRA account and delay taking RMD until they turn 70 1/2. Non-spouse beneficiaries simply take the RMD based on their own life expectancy. The only exception for a non-spouse beneficiary is if the deceased had already started taking RMD and the beneficiary is older; in that case the beneficiary could use the deceased person's

YOUTH IS NO EXCUSE FOR NOT HAVING A WILL

An August 2001 study conducted by FindLaw.com found that six in 10 American adults did not have a will. Of all the age demographics surveyed, younger adults were the least likely to have one.

Why is a will necessary and why should you have one even if you are young? You need a will because death doesn't discriminate by age. A will is a legal document that explains:

- Where you want the remainder of your estate's assets to go after debts and taxes are paid
- Who will oversee the execution of the will.
- It also may include who will care for your minor children. However, you may use a document called a declaration of guardianship to cover that contingency.

Without a will, the laws of your home state will determine how your property is distributed. Without it your children or other heirs may not receive the assets you intended for them to receive, the assets could be badly managed, your children could be placed with a different guardian than you had wanted, or your estate could pay more in taxes and legal fees than necessary.

You can write your own will to save money. But keep in mind that an improperly drafted or witnessed will may be rejected by the court as invalid, is open to being challenged by heirs, or may lack important information. State laws vary greatly, and your will must meet the requirements of your state. That's why it is a good idea to have an estate planning attorney draft the will.

There are several important points to keep in mind when drafting a will:

- **A will doesn't supersede named beneficiaries** for a Life insurance policy, a retirement account or property held in joint tenancy with right of survivorship.
- **A guardian should be chosen carefully.** The court will have to approve your selection, but in most instances, the person you name will be approved. Make certain the guardian is willing and physically capable of caring for your children. Determine that they have the financial resources, or that you will leave them the resources necessary to pay for the care of your children. It is a good idea to name a contingent guardian in the event the first person you selected has a change in health or financial circumstances.
- **The guardianship ends when your children turn 18 or 21.** At that time they gain control of

life expectancy to determine RMD.

Leaving the IRA to an individual can be particularly powerful when the beneficiary is much younger.

For example, let's assume you name your 20 year-old grandson as your IRA beneficiary. Based on the IRS single life tables, your grandson would only need to withdraw slightly more than 1.7% of the account for the initial distribution year, gradually increasing throughout his lifetime. This is far superior to distributing the full account balance within five years.

Name Names

If you have never named a beneficiary on your IRA account, you should designate one immediately. Of course, there are disadvantages to naming anyone as beneficiary. After the account holder dies, the beneficiary can do whatever he or she wishes with the money. This may mean taking the full balance of the account in spite of the account holder's plan for long-term, tax-deferred growth. The money could also find its way to the beneficiary's creditors, spouses, and ex-spouses. This makes choosing your beneficiary an important estate planning strategy.

any assets you've left them. If you wish to prevent this, you can establish a trust effective at your death that will manage the assets until your children reach the age at which you feel they should assume control.

- **An executor oversees the execution of the particulars of the will** and ensures all debts and estate taxes are paid, so choose someone you can trust. It is important to give the executor the power to carry out any duties necessary to properly execute your will, unless the state allows for independent executorships. Otherwise, the executor must obtain the court's permission, which results in needless delay and expense. Be sure to name a backup executor.
- **A will may be used to identify who is to receive personal property of sentimental value but little monetary value.** You may want to use a separate letter of instruction for this because it reduces the cost of rewriting the will each time you decide to make changes.
- **A will should take care to address potential estate taxes**, perhaps by establishing trusts upon your death. A poorly drafted will establishing a trust to protect some of your estate from taxes could, for example, result in impoverishing your spouse.

FOUR ESTATE PLANNING STRATEGIES YOU SHOULD CONSIDER

Although you may be aware of the 2010 estate tax repeal, and the scheduled re-instatement in 2011, you may not be aware of other aspects of estate planning still in effect that are extremely important to consider.

Create a will. The will is one of the only ways you have to ensure your assets are distributed to the people you deem worthy. Without a will, your state's laws will determine the distribution of your assets for you.

Create a living will, medical power of attorney, and financial power of attorney. A living will defines which life-saving medical procedures you want or don't want in the event that you are incapacitated. Medical power of attorney states which person you want to make medical decisions on your behalf, while a financial power of attorney stipulates who will make financial decisions, should you become unable to do so.

Don't forget about the annual gift tax exclusion. The best strategy to save estate taxes is to give (tax-free) up to $12,000 a year to each beneficiary you choose. This amounts to $24,000 a year with your spouse, given jointly to each of your children, grandchildren, or anyone else, without incurring a gift tax.You can also make unlimited gift tax-free payments for another person's tuition (tuition only, not room, board, supplies or books) or unreimbursed medical bills, without it counting towards the payer's lifetime gift exclusion, as long as such payments are made directly to the institution and not the recipient.

Consider lifetime giving. If you have sufficient funds to live on, you should consider a lifetime giving strategy, rather than waiting until your death to begin passing on your estate. This strategy has a few advantages: you can remove appreciating assets, such as common stock, from your estate. Also, if the gift is taxable, the money you use to pay the tax is also removed from your estate, reducing future estate taxes.

Designating where your assets go once you have passed is a difficult concept to consider, but it is extremely important that you seize the opportunity to plan this yourself, rather than allowing others, including the government, to decide for you.