

Here's a simple financial question: who is the beneficiary of your IRA? How about your 401(k), life insurance policy, or annuity?

You may be able to answer such a question quickly and easily. Or you may be saying, "You know ... I'm not totally sure." Whatever your answer, it is smart to periodically review your beneficiary designations.

Your choices may need to change with the times. When did you open your first IRA? When did you buy your life insurance policy? Was it back in the Eighties? Are you still living in the same home and working at the same job as you did back then? Have your priorities changed a bit – perhaps more than a bit?

While your beneficiary choices may seem obvious and rock-solid when you initially make them, time has a way of altering things. In a stretch of five or ten years, some major changes can occur in your life – and they may warrant changes in your beneficiary decisions.

In fact, you might want to review them annually. Here's why: companies frequently change custodians when it comes to retirement plans and insurance policies. When a new custodian comes on board, a beneficiary designation can get lost in the paper shuffle. (It has happened.) If you don't have a designated beneficiary on your 401(k), the assets may go to the "default" beneficiary when you pass away, which might throw a wrench into your estate planning.

How your choices affect your loved ones. The beneficiary of your IRA, annuity, 401(k) or life insurance policy may be your spouse, your child, maybe another loved one or maybe even an institution. Naming a beneficiary helps to keep these assets out of probate when you pass away.

Many people do not realize that beneficiary designations take priority over bequests made in a will or living trust. For example, if you long ago named a son or daughter who is now estranged from you as the beneficiary of your life insurance policy, he or she will receive the death benefit when you die, regardless of what your will states.¹

You may have even chosen the "smartest financial mind" in your family as your beneficiary, thinking that he or she has the knowledge to carry out your financial wishes in the event of your death. But what if this person passes away before you do? What if you change your mind about the way you want your assets distributed, and

are unable to communicate your intentions in time? And what if he or she inherits tax problems as a result of receiving your assets? (See below.)

How your choices affect your estate. Virtually any inheritance carries a tax consequence. Of course, through careful estate planning, you can try to defer or even eliminate that consequence.

If you are simply naming your spouse as your beneficiary, the tax consequences are less thorny. Assets you inherit from your spouse aren't subject to estate tax, as long as you are a U.S. citizen.² For example, a spouse can roll assets inherited from a 401(k) plan into an IRA without incurring taxes on the wealth transfer.³

When the beneficiary isn't your spouse, things get a little more complicated ... for your estate, and for your beneficiary's estate. If you name, for example, your son or your sister as the beneficiary of your retirement plan assets, the amount of those assets will be included in the value of your taxable estate. This might mean a higher estate tax bill for your heirs. And the problem will persist: when your non-spouse beneficiary inherits those retirement plan assets, those assets become part of his or her taxable estate, and his or her heirs might face higher estate taxes. Your non-spouse heir might also have to take required income distributions from that retirement plan someday, and pay the required taxes on that income.⁴

As a result of the Pension Protection Act, surviving spouses from same-sex couples may be allowed by employers to convert inherited retirement plan assets into inherited, traditional or Roth IRAs, avoiding taxes until those assets are withdrawn. This requires a direct transfer, not a rollover distribution.⁵

If you designate a charity or other 501(c)(3) non-profit organization as a beneficiary, the assets involved can pass to the charity without being taxed, and your estate can qualify for a charitable deduction.⁷

Are your beneficiary designations up to date? Don't assume. Don't guess. Make sure your assets are set to transfer to the people or institutions you prefer. Be sure to talk about it with the financial professional or estate planner you know and trust.



The Right Beneficiary
*Who have you chosen to inherit your assets?
It may be wise to review your choices.*
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Citations. ¹ seattlepi.nwsource.com/lifestyle/356213_consumer25.html

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