

Points of Law

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Wallace D. Cegavske, Attorney at Law
87102
Office 505 242-3444

302 Silver Ave SE

Albuquerque, NM

Fax 505 242-
3770

NOTE TO READERS

The good news is that the 2001 Proposed beneficiary rules for IRA distributions greatly simplify the Proposed 1987 rules that preceded them. The bad news is that it remains Proposed rule change in spite of the April 17, 2002 Federal Register notice of rule making. The rules substantially change the effect of beneficiary designations. Everyone should review the rules and their IRA beneficiary designations to ensure that the most satisfactory distribution possible can occur in the event of their death.

For example an 89 year old surviving spouse with more assets than needed might disclaim to his/her children. The net effect would be to remove the IRA from his/her estate and delay income taxation as the children would surely have a much longer life expectancy and be required to take much smaller minimum distributions.

Provided the beneficiary election for the IRA is written carefully with multiple primary and layers of contingent beneficiaries, great flexibility can be achieved.

DESIGNATED BENEFICIARY

When you die, minimum distributions from your IRA must be made, but the amounts vary. If there are designated beneficiaries the required minimums are determined based on the life expectancy of the designated beneficiary. For other beneficiaries, or if there is no beneficiary, other rules apply.

A Designated beneficiary must be an individual, such as a spouse or a child, or a qualified trust. A charity, estate, or a non-qualified trust cannot be a Designated beneficiary. Choosing designated beneficiaries can have a big impact on how quickly the assets must be distributed, and thus, of course, how quickly they are taxed.

The designated beneficiary will be determined as of the end of the year following your death - the prior rule provided that the designated beneficiary was determined as of your required beginning date.

For multiple designated beneficiaries, the minimum required distribution will be determined by the shortest life expectancy of any of the beneficiaries. To gain a longer distribution period, those with short life expectancies can be eliminated if they make a payout election or a disclaimer.

OPPORTUNITIES

The rules permit great flexibility. By delaying when the designated beneficiary must be chosen, planners can use disclaimers as late as December 31 of the year following death to determine the designated beneficiary.

OTHER BENEFICIARIES

If you die before the required beginning date and your estate becomes your beneficiary, except in limited circumstances, distribution must be completed in 5 years. For that reason, and others, your estate should not be the beneficiary.

Also, if you die before the required beginning date and a trust is named as a beneficiary, there are multiple requirements that must be strictly complied with or the same distribution within 5 years requirement arises. Those requirements include:

- Proper documentation
- Non-revocability requirements
- Clearly identified beneficiaries
- Proper documentation

Opportunities also exist to maximize benefit and minimize taxation through what are called stretch IRAs and through the use of charitable remainder trusts.

SUGGESTIONS

Beneficiary designations are clearly an important feature of any estate plan. They should be discussed thoroughly with an estate planner to assure that they are integrated with your estate plan.

Remember, the IRA is included in your estate for tax purposes. It is also taxed as received as ordinary income.

Careful designation of your beneficiaries and planning for the dates of required distributions can maximize the benefit from your plan.