

info sheet

Choosing beneficiaries for your IRA

At some point in your working career, you may be faced with having to decide what to do with a distribution from a 401(k) plan or another type of qualified retirement plan. Until that time, your retirement money had taken advantage of the tax-deferred benefits offered by such plans. However, once you change jobs or near retirement age, the assets may be subject to distribution requirements and possible taxation.

Making sure that you have made plans for your retirement assets is critical. A comprehensive financial and estate plan can help ensure that you are able to meet your financial needs after you retire. In addition, should you die before reaching retirement age, you can ensure the financial well being of your surviving beneficiaries.

The most common vehicle for shifting retirement plan assets at retirement is an Individual Retirement Account (IRA). After changing jobs or upon reaching retirement, you can roll over your retirement plan assets into an IRA. If you die before reaching retirement age, or before you establish an IRA, your plan account's designated beneficiary may be able to roll the assets into an IRA as well.

Typically, the IRA owner may name a spouse, child, trust, or charity as a beneficiary of his or her IRA.

All IRAs are subject to Required Minimum Distribution (RMD) rules established by the Internal Revenue Service. RMD rules state that there is a penalty if you do not take the required minimum distribution in any calendar year after you reach age 70½. The penalty imposed is a 50% excise tax on the difference between the amount required to be distributed and the amount actually distributed.

Generally, the IRA assets must start to be distributed by April 1st of the calendar year following the year in which the individual becomes age 70½.

Surviving spouse as beneficiary

If your surviving spouse is the designated beneficiary of your IRA, he or she can roll over the assets tax free into an IRA in his or her own name (IRA Rollover) or claim your IRA as his or her own account.

If your surviving spouse elects to treat your IRA as his or her own account or roll it over, he or she will not be required to start distributions until April 1st of the calendar year following the year in which he or she turns 70½. Your spouse may continue to make contributions to this IRA until distributions are required. If your spouse is already age 70½ at your death, distributions must start in the year after your year of death.

If your spouse needs income immediately, he or she may take distributions from a rollover IRA. However, distributions made before he or she reaches age 59½ will be subject to income tax and possible penalty taxes for early withdrawal. In this case, your spouse may want to consider taking distributions directly from your account, as distributions made to a beneficiary upon your death will be exempt from penalty taxes.

If your spouse chooses to take distributions from your IRA as a beneficiary rather than establishing an IRA in his or her own name, he or she will be required to take minimum distributions calculated over his or her own life expectancy beginning on or before the later of:

- December 31 of the calendar year immediately following the calendar year in which the IRA owner dies, or
- December 31 of the calendar year in which the IRA owner would have become 70½.

Multiple beneficiaries and segregated accounts

You may wish to name more than one beneficiary for your IRA. Generally, if you name more than one beneficiary, the life expectancy of the oldest beneficiary will be used for determining the distribution period. However, the account may be split up into separate accounts for each of the beneficiaries. Then each beneficiary would be able to take distributions based on his or her own life expectancy.

Spouse as beneficiary and family trust as secondary beneficiary

You may name your surviving spouse as the primary beneficiary of your IRA and a family trust as secondary beneficiary. Under this type of designation, your surviving spouse can keep part or all of the IRA if he or she needs it, or disclaim part or all of the IRA in order to fund the family trust.

In turn, the family trust can name all the children as beneficiaries and calculate the required minimum distribution for the oldest beneficiary. This strategy would allow the assets to build up in the account and defer the income tax until a later date (known as “stretching” the IRA*).

Making your retirement planning choices, particularly determining the beneficiaries for your retirement assets, is a crucial part of a comprehensive estate plan. Check with your investment professional about the beneficiary options that are right for your own financial and estate plan.

* For a discussion of the stretch IRA strategy, ask your investment professional for the MFS Heritage Planning infosheet “Stretch IRAs.”

For information about IRS regulations you should consider when planning your beneficiary strategy, ask your investment professional for the MFS Heritage Planning infosheet “Required Minimum Distribution Rules: A Snapshot” or visit our Web site at www.mfs.com.

This information sheet provides a brief discussion of the IRA beneficiary options. MFS does not provide legal or tax advice. Individuals should contact a qualified attorney or investment professional before finalizing any estate plans.

For further information

Gallea, Anthony M. *The Lump Sum Advisor*, Prentice Hall, 1999, 324 p., \$25.00.

Suttle, John C. and Slesnick, Twila. *IRAs, 401(k)s, and other Retirement Plans: Taking Your Money Out*, Nolo Press, 1998, 200 p., \$21.95.

Contact your investment professional for more information or to construct a personalized Heritage PlanningSM Profile to help your parents, your children, or yourself.

This material is not intended to replace the advice of a qualified attorney, tax adviser, investment professional, or insurance agent. Before making any financial commitment regarding the issues discussed here, consult with the appropriate professional.

