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CLIENT PLANNING GUIDE

Inherited Retirement Accounts

Key beneficiary-designation considerations for protecting the value passed to loved ones.

Why does it matter whom I name as the beneficiary of my retirement assets?

Who you name can affect how long inherited retirement funds may remain invested and the income-tax consequences for the beneficiary. Rules depend on the account, beneficiary category and circumstances.

Generally, estate planning aims to **(1) maximize the withdrawal time period because that maximizes the length of time that assets can continue to grow within the retirement account and (2) achieve the best possible income tax situation for the beneficiary.**

Maximizing the withdrawal period allows retirement assets to grow tax-deferred for longer, increasing their potential value to the beneficiary. Spreading smaller withdrawals over the longest period permitted can also minimize income taxes and help prevent distributions (except from Roth accounts, which generally receive different tax treatment) from pushing the beneficiary into a higher tax bracket.

GENERAL WITHDRAWAL TIME FRAMES

- ☐ Nonhuman beneficiary/Charity: generally 5 years.
- ☐ Designated beneficiary: generally 10 years.
- ☐ Eligible designated beneficiaries: may use life-expectancy rules. Examples listed include a surviving spouse, the participant's minor child (until age 21), a disabled or chronically ill beneficiary, and a person not more than 10 years younger than a plan participant.

QUESTIONS TO REVIEW WITH YOUR TEAM

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| <ul style="list-style-type: none"> ☐ Could withdrawal timing affect the beneficiary's taxable income or push distributions into a higher tax bracket? ☐ If married, do plan rules require spousal consent or naming a spouse as primary beneficiary—particularly for certain ERISA-governed plans? ☐ Would a Roth conversion support your goals? Compare potential beneficiary tax benefits with taxes you may owe on conversion now. | <ul style="list-style-type: none"> ☐ Are annual required minimum distributions (RMDs) required, or can withdrawals be timed differently under the applicable rules? ☐ If naming a trust, has the attorney considered its structure and countable beneficiaries to seek appropriate treatment? ☐ Are beneficiary designations coordinated with the overall estate plan and the people or causes you want to benefit? |
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FREQUENTLY ASKED QUESTIONS

Are there rules about whom I can, or cannot, name as the beneficiary of my retirement assets?

Certain types of retirement assets (i.e., those governed by federal Employee Retirement Income Security Act of 1974 (ERISA) rules, such as 401(k)s) may require you to name your

spouse as the primary beneficiary if you are legally married. Unmarried individuals are not subject to such restrictions. In addition, non-ERISA accounts (e.g., individual retirement accounts) are not usually subject to such limitations. However, among eligible designated beneficiaries, spouses often receive the best possible treatment for inherited retirement assets because they can usually "roll over" the funds.

What if I want to name a trust as the beneficiary of my retirement assets?

By default, a trust is a nonhuman beneficiary, which generally has only five years to withdraw the funds. However, there is a workaround! Your attorney can design your trust in special ways to ensure that distributions to your trust get the best possible treatment. Thoughtful trust design involves careful consideration of who the "countable beneficiaries" of your trust are and how your trust is structured to optimize both the withdrawal time period and the income tax outcome.

Could doing a Roth conversion now be helpful?

Yes, this conversion could help achieve your goals, but there is more to consider. Remember, distributions from a Roth account are not subject to income tax when those funds are later withdrawn because those funds are subject to income taxation before they are contributed to the retirement account. So, by doing a Roth conversion, you can ensure that your beneficiaries will not be subject to income tax on their withdrawals from an inherited Roth retirement account, but it may mean that you have to pay taxes now on the amount you convert.

How should I proceed?

Confer with a knowledgeable, experienced estate planning attorney, and include your financial advisor or any other professionals who assist you. Together, they can gather all the relevant information about your assets so that your attorney can prepare the right sort of plan to accomplish your goals and provide the greatest benefit to your loved ones.

PLANNING POINTS TO REMEMBER

- ☐ Longer tax-deferred growth may benefit beneficiaries, while withdrawals from traditional retirement assets are generally taxable; Roth distributions may receive different treatment.
- ☐ Spouses may have options, such as rolling over eligible inherited funds, that differ from other beneficiaries.
- ☐ Do not rely on a general timeline alone—confirm current rules for the specific account and beneficiary.

Next step: review your retirement assets with an experienced estate planning attorney and your financial advisor or tax professional.

GRAY LAW FIRM, LLC | Contact us to schedule a consultation

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