



# ED SLOTT'S IRA ADVISOR

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## TAX & ESTATE PLANNING FOR YOUR RETIREMENT SAVINGS

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### Guest IRA Expert

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## Practical Issues When an IRA Owner Dies

The death of an IRA owner raises complicated legal issues. Often, these issues are mishandled – *and the consequences can be extremely costly*. The problems may be especially acute when the IRA owner's spouse is the sole beneficiary, which frequently is the case. Often, the surviving spouse will be in shock, not knowing what to do or whom to ask for advice.

Increasingly, IRAs are being left to a trust. (So-called IRA trusts might become even more prevalent if the federal estate tax is abolished as President Trump has proposed, because many attorneys may add IRA trusts to their practice.) Using a trust can create more opportunities for errors.

For advisors, the solution is to remain diligent. When a client dies, follow up on the IRA or IRAs held by that individual to assist with implementation of the post-death IRA distribution rules. Make sure that someone – *you the financial advisor, the client's attorney, or accountant* – is quarterbacking the process so that all required actions are taken and decisions are made thoughtfully.

**Taking the unpaid RMD, if any, as well as making a prompt transfer can be difficult, especially for a recent widow(er).**

### Year-of-Death Distributions

In many cases, the deceased IRA owner will be over age 70½, thus taking required minimum distributions (RMDs). If so, an RMD will be required for the year of death.

**Example:** Sam, age 85, dies in November 2017 and has not taken any of his RMDs for this year. (That's often the case.) If Sam's beneficiary is his wife, Sue, then Sue is responsible for taking the RMD for 2017, or she may owe a 50% penalty.

Calculating the RMD obligation and making a timely payment can be difficult, especially for a recent widow or widower. Ideally, one of Sue's advisors will contact the IRA custodian or custodians, determine what paperwork is necessary, and see that the RMD is distributed to Sue. *Note that the IRA custodian may not make this distribution, after an advisor's phone request.*

Generally, a letter of authority from the IRA beneficiary is required. The entire process might take months. It includes taking any unpaid RMDs, transferring the decedent's IRA to the surviving spouse's IRA, and naming new beneficiaries, such as their children.

As a result of such delays, Sue might die before transferring Sam's IRA into her own IRA and naming their children as beneficiaries. In that case, the account could pass to Sue's estate or to a default beneficiary.

Either way, the successor IRA beneficiary would use Sue's remaining single life expectancy, and RMDs would be accelerated. The ability to stretch the IRA over their children's life expectancies would be lost, potentially costing large amounts of tax-deferred buildup.

## Default Beneficiaries

Advisors should realize that many major financial firms have default beneficiary provisions in their IRA adoption agreements for both primary and successor beneficiaries. Thus, if someone inherits an IRA and dies before naming their own beneficiaries, the default beneficiary will get the money – *and that person might not be the desired recipient.*

**Example:** Marjorie dies and leaves her IRA to her son Eddie. Then Eddie dies without naming a beneficiary and the IRA custodian’s adoption agreement states the default beneficiary is his spouse. However, Eddie would not have wanted his second wife, Paula, to get the IRA. Other assets are provided for her under a prenuptial agreement, in which she waived her rights to any retirement accounts. Nevertheless, under the IRA custodian’s adoption agreement Paula would be the default beneficiary, rather than Eddie’s children from a prior marriage. If Eddie had known about this, he would have used the financial firm’s form to name his children as successor beneficiaries.

Eddie’s children or Eddie’s estate might have to go to court, in an attempt to claim Eddie’s IRA. However, IRS frequently does not accept a state court’s order to change a beneficiary. To avoid such problems, as well as significant litigation costs, advisors should see that clients’ IRAs, including inherited IRAs, are handled properly. In this example, after Eddie inherits the IRA, it’s vital to make sure that he has a successor beneficiary form that names his children on file with the IRA institution. This issue could affect millions of inherited IRA accounts that have default beneficiary provisions in their IRA adoption agreements.

A similar problem may crop up if IRA owners neglect to fill out their beneficiary form. A surviving spouse could have some physical or mental condition that hampers decision making. To protect against such possibilities, advisors might suggest that elderly clients execute a power of attorney, naming a trusted individual as their agent authorized to make financial decisions on their behalf.

A power of attorney may be especially vital for a recent widow or widower. However, a power of attorney might encounter obstacles, after the death of an IRA owner. IRA custodians may not honor the agent’s right to select beneficiaries of the surviving spouse’s IRA.

Anticipating such problems, I have a special power of attorney form, illustrated below, that I use for clients when deemed necessary. This form (and often state law) specifically gives the agent the right to transfer the IRA to the spouse’s name, if indicated, and to distribute RMDs to the surviving spouse.

This special power also allows the agent to appoint beneficiaries of the surviving spouse’s IRA. To avoid any appearance of self-dealing, the special power might say that the agent can “pick the following beneficiaries,” naming the people the agent would be able to select.

## Trust Troubles

Still more issues may arise if an IRA trust is the intended beneficiary. That is, Jim would work with an attorney to create the Jim Jones Trust. At Jim’s death, this trust would be Jim’s IRA beneficiary. Jim’s wife, Jan, would be the beneficiary of the trust, receiving distributions passed from the IRA to the trust and on to Jan. Thus, the

## Power of Attorney Sample Form\*

In the event that I survive my spouse, \_\_\_\_\_ **X** \_\_\_\_\_,  
and I am designated as the beneficiary of \_\_\_\_\_ **X** \_\_\_\_\_’s  
individual retirement account, then in that event and to the extent  
permitted by law, my agent can transfer said individual retirement  
account assets to an individual retirement account maintained in my  
name, \_\_\_\_\_ **Y** \_\_\_\_\_ and name the following beneficiaries,  
including my agent, \_\_\_\_\_ **Z** \_\_\_\_\_, as beneficiaries of my  
individual retirement account.

\*This is just suggested language and should be reviewed by counsel and modified as required by state law.  
For example, New York State law requires this to be done in a special format which is different from other states.

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inherited account would include the Jim Jones Trust for the benefit of (F/B/O) Jan Jones in its title. This arrangement might serve to protect the funds in the IRA from being squandered by the beneficiary, if that beneficiary is in failing mental or physical health.

It's critical when setting up such an IRA trust to specify on the beneficiary form that the trust will be the IRA beneficiary only if Jan survives Jim. The beneficiary form should list all contingent beneficiaries (such as their children) in case Jan should predecease Jim, and the trust is no longer necessary. Assuming that the attorney drafting the trust foresees such contingencies, the trust beneficiary may be well-served as he or she advances in age.

From what I've seen, in many cases, the IRA trust may not be named on the IRA beneficiary form in a timely manner. Dozens of times, I have discovered that the IRA beneficiary forms have not been done promptly. All that time and effort and expense in the trust creation will be wasted if the IRA RMDs don't flow into the IRA trust as the designated beneficiary if the IRA owner dies before updating his beneficiary form.

Therefore, I insist that a new IRA beneficiary form, naming the IRA trust, is put into play on the day the IRA trust is finalized. Some advance planning may be necessary to see that the IRA custodian is notified promptly. If the IRA trust is not the designated beneficiary at the IRA owner's death, then the IRA would be left to the individual previously named on the beneficiary form, or perhaps to the IRA owner's estate. As mentioned above, the opportunity for a valuable stretch IRA might wind up being lost.

To qualify for stretch IRA tax benefits, a copy of the trust document must be provided to the IRA custodian by October 31<sup>st</sup> of the year following the year of the IRA owner's death. Naming the trust also can be critical. The beneficiary form should refer to the Jim Jones Trust, without including the words "deceased" or "IRA" in the title of the trust.

## A Minor Beneficiary Can Be a Major Headache

Some IRA owners choose to name a minor, such as a child or grandchild, as the IRA beneficiary. A young beneficiary will have a long life expectancy, which can lead to extraordinary wealth creation from decades of tax deferral. However, some financial firms won't pay IRA money to a minor named as IRA beneficiary. The minor's family may have to go to court to get a guardian of the property appointed for as long as the minor is under age.

To deal with any possible problem, care should be taken with the beneficiary form. One approach is to include language to deal with a beneficiary who might be under age. The form might state:

*"If the beneficiary is not 18 or 21 or 25 (depending on relevant state law), my executor can name a custodian until the beneficiary comes of age, under the Uniform Transfers To Minors Act (UTMA), and the IRA would be payable to the UTMA account."*

The executor might be able to name any adult person, including himself or herself, to serve as custodian for the minor. Again, it would be up to the IRA owner's advisors to see that the proper procedures are followed, to minimize potential perils. ■

**Seymour Goldberg, CPA, MBA, JD** is the senior partner in the law firm of Goldberg & Goldberg, P.C. in Long Island, New York. He was formerly associated with the Internal Revenue Service. He conducted many continuing education programs with the IRS and other organizations on the retirement distribution rules. He has written two books on IRA issues for the American Bar Association which can be found in law school libraries throughout the United States. They are *Inherited IRAs, What Every Practitioner Must Know, 2017 Edition* and *IRA Guide to IRS Compliance Issues, Including IRA Trust Violations*, call 800-285-2221 or visit [shopaba.org](http://shopaba.org) for further details. Mr. Goldberg can be reached at 516-222-0422 or by email at [info.goldbergira@gmail.com](mailto:info.goldbergira@gmail.com).