

A Key Part of Your Estate Plan: The Beneficiary Designation

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After you have signed your estate planning documents, you still have more work to do. Where will you keep original documents? Who will get copies? But here's a topic that too often gets overlooked: the beneficiary designation.

What is at issue

Perhaps your will or trust directs that a particular bank account is to be distributed to a particular person. You may not realize that a beneficiary designation on the account will override your estate plan. Did you put your daughter's name on the account as beneficiary when you set it up? Are you sure?

Beneficiary designations are commonplace on many kinds of assets. They are possible on almost any type of property. Among the asset types that often include beneficiary designations:

Life insurance, of course, almost always names a beneficiary

Individual retirement accounts (IRAs), along with other retirement accounts and pensions, need to list a beneficiary for tax reasons — and they almost inevitably do

Individual stock certificates and bonds can have a beneficiary, and so can brokerage and online investment accounts (under Arizona law, this is called a "transfer on death" or TOD provision)

Bank and other financial accounts may have a "pay on death" (POD) or "in trust for" (ITF) designation

In Arizona, even vehicle titles can list a beneficiary

In a growing number of states, real estate can have a beneficiary, using what Arizona law calls a "beneficiary deed"

Who you should list as beneficiary

This, of course, is the important consideration. Should you name your estate, or your trust, as beneficiary on your bank accounts, your life insurance, your retirement accounts and all the other things you could list? Or should you just list the people who will inherit your estate — that is, the beneficiaries named in your will or trust?

Sadly, there is no easy and universal answer. This is going to require some individualized discussion.

Some people use extensive beneficiary designations to make sure their estate will avoid probate, without having to incur the cost of creating (and funding) a trust. That can work fine, but requires extra vigilance to make sure those beneficiary designations remain current over the years.

Even people who execute a trust may use beneficiary designations to transfer assets to the trust upon death. That can be very effective, and makes the process easier — but can unnecessarily subject those assets to the trust owner's creditors or increased tax liabilities.

If you do rely on beneficiary designations, it is important to review and update those designations every few years. Do not rely on your memory — ask each account holder to tell you who they show as beneficiary. We have seen people surprised to learn who they named as beneficiary — perhaps more often than their memory has been confirmed.

What can go wrong?

There are a number of things that can change your estate plan unintentionally. Here are some we see regularly:

Divorce:

If you have named a spouse as beneficiary and then get divorced, Arizona law says that the beneficiary designation is automatically changed. Except when it is not. And besides, the account custodian might have rules that it thinks override Arizona's law, or apply another state's law. That's what happened in the July 14, 2017, federal court of appeals case of *Lazar v. Kroncke*, applying Arizona's law to a Charles Schwab IRA account. We will probably write about that case in more detail next week, but the key message for now is this: George Kroncke could have solved future legal problems by revisiting his beneficiary designation sometime between his 2008 divorce and his death in 2012.

Broker changes:

Here's one we see from time to time. You've had a stockbroker for years, and you love working with her. She's smart, she's responsive, and she has had success with your accounts. Recently she moved to a new company, and asked you if you want to move your accounts. You did want to, and she made it easy.

But here's something you didn't know. When she left her old company, the only thing she took with her was her client list. She didn't have access to your account details, including the beneficiary designations you painstakingly set up five years ago. Your new account might not have the same, or the correct, beneficiary designations.

Family changes:

Perhaps you named your sister as beneficiary on an account. Sadly, she died a couple years ago. Does that mean the share you had designated to her goes to her children, or her surviving spouse, or the other beneficiaries you named? You may be clear about what you want, or even about what you think will happen — but why not update your beneficiary designations and make sure they are correct?

The same thing will be true for other kinds of family changes. Maybe one of your children has married, but you aren't wild about the new in-law. Or your child married and then adopted step-children. How do you want to handle those situations? Because naming your child as beneficiary may or may not accomplish your wishes with regard to successors beneficiaries.

Here's a small piece of good news: if your daughter has married (or divorced) and changed her name, you probably don't have to update the beneficiary designation. Same for your son's new address. But their life changes might be a good reason to revisit your estate plan — and your beneficiary designations.

Special cases

Beneficiary designations for retirement accounts like pensions, IRAs and 401(k) accounts pose special problems. They may be covered by federal rules that limit the kinds of changes you can make (unless you get your spouse's approval). There will also be tax considerations. Most of the tax concerns will affect your beneficiaries, not you — but it can still be difficult to decide on the proper beneficiary designation.