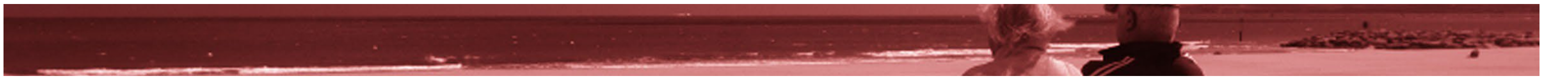


Newsletter Fall 2025

Choosing a Beneficiary for Your IRA or 401(k)

Selecting beneficiaries for retirement benefits is different from choosing beneficiaries for other assets such as life insurance. With retirement benefits, you need to know the impact of income tax and estate tax laws in order to select the right beneficiaries. Although taxes shouldn't be the sole determining factor in naming your beneficiaries, ignoring the impact of taxes could lead you to make an incorrect choice.

In addition, if you're married, beneficiary designations may affect the size of minimum required distributions to you from your IRAs and retirement plans while you're alive.

Paying income tax on most retirement distributions

Most inherited assets such as bank accounts, stocks, and real estate pass to your beneficiaries without income tax being due. However, that's not usually the case with 401(k) plans and IRAs.

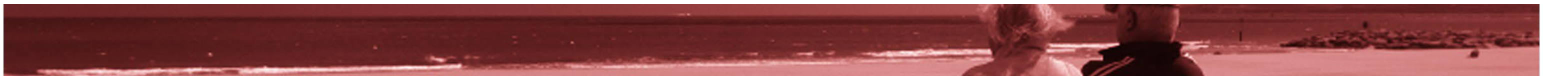
Beneficiaries pay ordinary income tax on distributions from pre-tax 401(k) accounts and traditional IRAs. With Roth IRAs and Roth 401(k) accounts, however, your beneficiaries can receive the benefits free from income tax if all of the tax requirements are met. That means you need to consider the impact of income taxes when designating beneficiaries for your 401(k) and IRA assets.

For example, if one of your children inherits $100,000 cash from you and another child receives your pre-tax 401(k) account worth $100,000, they aren't receiving the same amount. The reason is that all distributions from the 401(k) plan will be subject to income tax at ordinary income tax rates, while the cash isn't subject to income tax when it passes to your child upon your death.

Similarly, if one of your children inherits your taxable traditional IRA and another child receives your income-tax-free Roth IRA, the bottom line is different for each of them.

Naming or changing beneficiaries

When you open up an IRA or begin participating in a 401(k), you are given a form to complete in order to name your beneficiaries. Changes are made in the same way — you complete a new beneficiary designation form. A will or trust



does not override your beneficiary designation form. However, spouses may have special rights under federal or state law. Your plan's website may also have an option to update your beneficiary information.

It's a good idea to review your beneficiary designation form at least every two to three years. Also, be sure to update your form to reflect changes in financial circumstances. Beneficiary designations are important estate planning documents. Seek legal advice as needed.

Designating primary and secondary beneficiaries

When it comes to beneficiary designation forms, you want to avoid gaps. If you don't have a named beneficiary who survives you, your estate may end up as the beneficiary, which is not always the best result.

Your primary beneficiary is your first choice to receive retirement benefits. You can name more than one person or entity as your primary beneficiary. If your primary beneficiary doesn't survive you or decides to decline the benefits (the tax term for this is a disclaimer), then your secondary (or "contingent") beneficiaries receive the benefits.

Having multiple beneficiaries

You can name more than one beneficiary to share in the proceeds. You just need to specify the percentage each beneficiary will receive (the shares do not have to be equal). You should also state who will receive the proceeds should a beneficiary not survive you.

In some cases, you'll want to designate a different beneficiary for each account or have one account divided into subaccounts (with a beneficiary for each subaccount). Keep in mind that, due to legislation passed at the end of 2019 (the SECURE Act), most non-spouse beneficiaries are required to empty their inherited retirement accounts within 10 years (previously, they could take distributions according to their life expectancies). Exceptions include minor children, those who are not more than 10 years younger than the account owner (such as a close-in-age sibling), and individuals who meet the IRS's definition of chronically disabled. (Once a minor child reaches age 21, the 10-year rule applies.)

Avoiding gaps or naming your estate as a beneficiary

There are two ways your retirement benefits could end up in your probate estate. Probate is the court process by which assets are transferred from someone who has died to the heirs or beneficiaries entitled to those assets.

First, you might name your estate as the beneficiary. Second, if no named beneficiary survives you, your probate estate may end up as the beneficiary by default. If your probate estate is your beneficiary, several problems can arise.

If your estate receives your retirement benefits, the opportunity to maximize tax deferral by spreading out distributions may be lost. In addition, probate can mean paying attorney's and executor's fees and delaying the distribution of benefits.

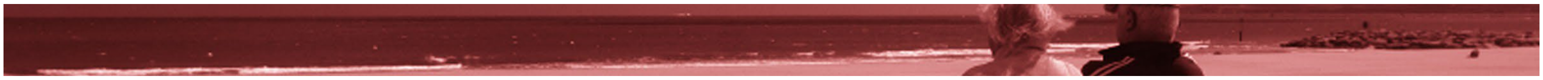
Naming your spouse as a beneficiary

When it comes to taxes, your spouse is usually the best choice for a primary beneficiary.

A spousal beneficiary has the greatest flexibility for delaying distributions that are subject to income tax. In addition to rolling over your 401(k) or IRA to their IRA or plan, a surviving spouse can generally decide to treat your IRA or plan account as their own.

These options can provide more tax and planning options.

If your spouse is more than 10 years younger than you, then naming your spouse can also reduce the size of any required taxable distributions to you from retirement assets while you're alive. This can allow more assets to stay in the retirement account longer and delay the payment of income tax on distributions.



Although naming a surviving spouse can produce the best income tax result, that isn't necessarily the case with estate taxes. At your death, your spouse can inherit an unlimited amount of assets and defer federal estate tax until both of you are deceased (note: special tax rules and requirements apply for a surviving spouse who is not a U.S. citizen). If your spouse's taxable estate for federal tax purposes at his or her death exceeds the applicable exclusion amount, then federal estate tax may be due. In other words, one possible downside to naming your spouse as the primary beneficiary is that it may increase the size of your spouse's estate for estate tax purposes, which in turn may result in an unexpected tax burden when your spouse dies.

Naming other individuals as beneficiaries

You may have some limits on choosing beneficiaries other than your spouse. No matter where you live, federal law dictates that your surviving spouse be the primary beneficiary of your 401(k) plan benefit unless your spouse signs a timely, effective written waiver. And if you live in one of the community property states, your spouse may have rights related to your IRA regardless of whether he or she is named as the primary beneficiary.

Keep in mind that a nonspouse beneficiary cannot roll over your 401(k) or IRA to their own IRA. However, a nonspouse beneficiary can directly roll over all or part of your 401(k) benefits to an inherited IRA.

Naming a trust as a beneficiary

You must follow special tax rules when naming a trust as a beneficiary, and there may be income tax complications. Seek legal advice before designating a trust as a beneficiary.

Naming a charity as a beneficiary

In general, naming a charity as the primary beneficiary will not affect required distributions to you during your lifetime. However, after your death, having a charity named with other beneficiaries on the same asset could affect the tax-deferral possibilities of the noncharitable beneficiaries, depending on how soon after your death the charity receives its share of the benefits.

Estate as Beneficiary of Traditional IRA or Retirement Plan

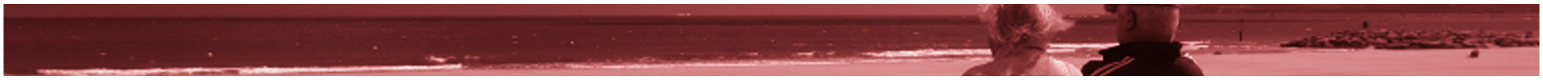
What is it?

Generally, following your death, your nonretirement assets will pass according to your will or trust or beneficiary designations (e.g., life insurance). If you do not have a will or trust or there is a gap in your beneficiary designations, the laws of your state (or the state where you own real property) will generally determine your heirs.

With IRAs and employer-sponsored retirement plans, when you die, the remaining funds generally pass directly to the beneficiary (or beneficiaries) you have designated. Spouses, children and grandchildren, trusts, and charities are common beneficiary choices. However, if you have a gap in your beneficiary designations, your estate may become the "default" beneficiary of your IRA and/or retirement plan benefits. This could occur, for example, if all of your designated beneficiaries die before you, and then you die before naming a new beneficiary.

With your estate as the beneficiary of your IRA or plan, the money in the account is first distributed to your estate, and then passes to your heirs according to the terms of your will. Having your estate as beneficiary is usually the worst possible beneficiary choice in terms of tax implications. In addition, you will sacrifice some planning options and potentially expose the retirement funds to extra fees, risks, and creditors.

Caution: *This discussion applies to traditional IRAs and employer-sponsored retirement plans. Special considerations apply to beneficiary designations for Roth IRAs.*



Having your estate as beneficiary will not affect required minimum distributions during your life

Under federal law, you must begin taking annual required minimum distributions (RMDs) from your traditional IRA and most employer-sponsored retirement plans (including 401(k)s, 403(b)s, 457(b)s, SEPs, and SIMPLE plans) by April 1 of the calendar year following the calendar year in which you reach age 73 (age 75 if you reach age 73 after 2032), known as your "required beginning date." With employer-sponsored retirement plans, you can delay your first distribution from your current employer's plan until April 1 of the calendar year following the calendar year in which you retire if (1) you retire after age 73 (age 75 if you reach age 73 after 2032), (2) you are still participating in the employer's plan, and (3) you own 5% or less of the employer.

Your choice of beneficiary generally will not affect the calculation of your RMDs during your lifetime unless your spouse is your sole designated beneficiary for the entire distribution year, and he or she is more than 10 years younger than you. But note, however, that having your estate as beneficiary will generally result in limited options (and the fastest possible payout) for required post-death distributions. See below for additional information.

Caution: *The calculation of RMDs is complex, as are the related tax and estate planning issues. For more information, consult a tax professional.*

Advantages of having your estate as beneficiary

There are virtually no advantages to having your estate as the beneficiary of your traditional IRA or retirement plan.

Disadvantages of having your estate as beneficiary

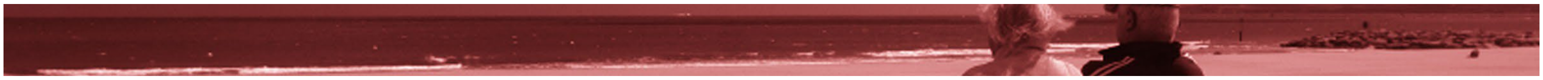
Post-death distribution options are limited and generally unfavorable

If your estate ends up as your IRA or retirement plan beneficiary at your death (either because you intentionally named your estate as beneficiary, or by default because you died with no living individual named as a beneficiary), you will be treated as if you died without any designated beneficiary. Required post-death distributions from the account will therefore have to be made at the fastest rate possible, potentially increasing the total income tax liability on the funds. And the more rapidly the funds must be distributed from the IRA or plan, the less time they have to continue growing in a tax-deferred environment. Here are the specific rules you should be familiar with:

- If you die prior to your required beginning date for RMDs with your estate as beneficiary, the IRA or plan funds must be distributed within five years after your death (the "five-year rule").
- If you die after your required beginning date for RMDs with your estate as beneficiary, the IRA or plan funds must be distributed over your remaining single life expectancy, calculated in the year of death (maximum of about17 years)

Note: *The 5-year period for defined contribution plans (other than Section 457 plans for non-governmental tax-exempt organizations) and IRAs is determined without regard to calendar year 2022. Thus, if the decedent died in 2017 to 2021 and distributions are subject to the 5-year rule, 2022 would be within the 5-year period and the 5-year period would effectively be extended to 6 years.*

If instead you named a spouse, child, other individual, or qualifying trust as beneficiary, post-death distribution options would be more favorable. For decedents dying before 2020, these beneficiaries would generally have the option of taking required post-death distributions over a longer period by using their own remaining life expectancy. For decedents dying after 2019, the life expectancy method can only be used if the designated beneficiary is an eligible designated beneficiary. An eligible designated beneficiary is a designated beneficiary who is the spouse or a minor child of the IRA owner or plan participant, a disabled or chronically ill individual, or other individual who is not more than ten years younger than the IRA owner or plan participant (such as a close-in-age sibling). (Spouses have more options, such as the ability to roll over the inherited funds into the spouse's own IRA or plan.) A longer post-death payout period will help spread out the income tax bill on the money, and further prolong tax-deferred growth.



Tip: *In the case of a qualifying trust as beneficiary of an IRA or plan, if the election is made to base post-death distributions on the beneficiary's life expectancy, the oldest beneficiary of the trust (i.e., the one with the shortest life expectancy) generally must be used for this calculation.*

The funds will have to pass through probate

If you die with your estate as the beneficiary of your IRA or retirement plan, the funds will have to pass through probate before being distributed to the heirs of your estate. Probate is the court-supervised process of administering an estate and also possibly proving a will to be valid. It is sometimes a costly, time-consuming process that is open to public scrutiny, and may also needlessly expose the retirement funds to creditors. However, if you designate an individual or a qualifying trust as the beneficiary of your IRA or retirement plan, the inherited funds will pass directly to that beneficiary without having to go through probate. This is often a compelling reason not to name your estate as beneficiary of your IRA or plan.

Estate tax issues

You may be concerned about possible estate tax issues if you expect the value of your taxable estate to exceed the federal applicable exclusion amount. After your death, the funds remaining in your IRA or retirement plan will be included in your taxable estate to determine if any federal estate tax is due. This is generally true regardless of whether you have named your estate, an individual, or a trust as beneficiary. In addition to federal estate tax, your state may impose a state death tax.

Caution: *Estate taxes and other estate planning issues are highly technical areas. Be sure to seek professional assistance from a qualified estate planning attorney.*

IMPORTANT DISCLOSURES

AMI Benefit Plan Administrators, Inc. does not provide investment, tax, legal, or retirement advice or recommendations. The information presented here is not specific to any individual's personal circumstances.

To the extent that this material concerns tax matters, it is not intended or written to be used, and cannot be used, by a taxpayer for the purpose of avoiding penalties that may be imposed by law. Each taxpayer should seek independent advice from a tax professional based on his or her individual circumstances.

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