

What is the importance of naming a beneficiary to my 401(k) account?

Understanding Beneficiary Designations



Key Point

The key to your beneficiary designations is remembering to update them as the people in your life change. For example, if you have children, change your marital status, or a beneficiary dies, you will need to update your designations.

What is a beneficiary?

A beneficiary is a person or an entity that receives money or other benefits from a benefactor (you) after your death. In the case of your 401(k), your beneficiaries will receive the assets in the account after your death, subject to the appropriate taxes. 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.

Why are beneficiaries important?

If you don't designate a beneficiary, then your 401(k) savings will be subject to probate, which means the state will decide who receives the proceeds of your account upon your death. You thereby have not exercised your right to direct your savings to those whom you wish to receive it.

Furthermore, your heirs will incur unnecessary legal expenses, time and trouble in probating your 401(k) account, or seeing it through the state's process. The exception is that if you are married, federal law states that your account's beneficiary is automatically your spouse, whether you designated him/her or not.

Can I name more than one beneficiary?

You certainly can. You can designate, by percentage, how much of your account is allotted to each beneficiary.

What is a primary and what is a secondary or contingent beneficiary?

Primary beneficiaries will receive the amount of the proceeds of your 401(k) as long as they are alive (and you are deceased). In case your primary beneficiary is deceased when you die, it is customary to designate secondary or contingent beneficiaries. You can likewise name more than one secondary or contingent beneficiary. As with your primary beneficiary designations, you will allocate the percentage of the whole you want to be awarded to each beneficiary.

What are some important considerations for designating beneficiaries?

Married. By federal law, your spouse is automatically your 401(k) beneficiary. For the record, you should nevertheless designate your spouse on your beneficiary designation forms. Your spouse must officially "waive" the right to be your beneficiary in order for you to elect alternative beneficiaries. To do so, your spouse must sign a spousal waiver to his/her right as the legal beneficiary of your 401(k).



Take Action

To change beneficiaries on your 401(k) account, request the "Beneficiary Change Form" from your company's plan administrator.

Separated. Be aware that your spouse remains your legal beneficiary unless and until you are divorced, unless your spouse has waived that right by signing the spousal waiver described above.

Single Parent. Be aware that if you've named your children as beneficiaries and you remarry, your new spouse is the automatic primary beneficiary of your 401(k) unless he/she waives that right by signing the spousal waiver.

Designating Children as Beneficiaries. If they're minors, the courts will likely appoint a trustee or guardian to manage your 401(k) proceeds on their behalf unless you have specified a trustee (person or institution) and named that trust as the children's beneficiary. Doing so will hasten the process by which the money can be transferred and invested for your children's benefit. In addition, you can set up a trust to manage your 401(k) proceeds on your children's behalf even if they are not minors. A trust must meet IRS requirements to serve as a designated beneficiary, so be sure to consult a tax advisor.

Domestic Partner. If you're not married but a domestic partner, designating your partner as your 401(k) beneficiary can help prove legitimacy of your status as domestic partners. Your 401(k) beneficiary designation of your partner may be supplied as evidence that you should qualify for domestic partner health benefits or qualify as registered domestic partners, in cities where applicable.

What are some examples of beneficiary designations?

A Married Woman: She may designate her husband as the primary beneficiary of her 401(k) account (by law, he is automatically) and designate her two children as 50% / 50% secondary or contingent beneficiaries.

A Young Single Man: He may designate his mother and father as 50% / 50% primary beneficiaries of his 401(k) account, and designate his four siblings as 25% / 25% / 25% / 25% secondary or contingent beneficiaries.

A Divorced Man Nearing Retirement: He may designate his two children as 50% / 50% primary beneficiaries, and his four grandchildren as 25% / 25% / 25% / 25% secondary or contingent beneficiaries.

Do my beneficiary designations have to agree with my will?

They do not. The beneficiary designations you make on your 401(k) plan will trump or overrule your will. Therefore, you can update your 401(k) beneficiaries without having to update your will, and these designations will be honored upon your death.

In what other types of personal finance situations do I designate beneficiaries?

Life insurance policies always require beneficiary designations. So if you are changing your beneficiaries on your 401(k) plan, be reminded that you may also want to change them on your life insurance policies.

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