



# Inherited IRAs

Let Your Beneficiaries Stretch Your IRA Assets Over *Their* Life Expectancies

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**The message regarding the need to save** for retirement is sinking in. More and more of us are putting money aside using vehicles such as IRAs and employer-sponsored retirement plans — like 401(k)s — in order to supplement our retirement savings. However, while these savings plans can be an important vehicle for funding your retirement years, they can also be an important part of the legacy you leave to your loved ones.

Therefore, it's important to know what happens to the assets in these plans when they are inherited and the options that will be available to your beneficiaries. For instance, did you know that when your beneficiaries inherit this money, they could be faced with a potentially large tax burden?

Fortunately, the law provides beneficiaries of IRAs, 401(k)s, and other employer-sponsored retirement plans some flexibility that can ease this burden. Spouses can generally transfer this money into an IRA in their own name.

Non-spouse beneficiaries, however, do not have this option. But they can receive the money slowly, through distributions taken over their own life expectancies (thereby spreading out the tax burden over a longer period of time), by rolling this money into a vehicle called an **Inherited IRA** (also sometimes called a “stretch IRA”).

## Who Will You Name?

You can name, as your beneficiary, your spouse, children, grandchildren, another individual, or favorite charity, or set up a trust — that's a choice you make. No matter whom you choose, though, it's important that you designate a choice and complete the appropriate documentation. If you don't, the tax consequences for your beneficiaries could be devastating.

If you have the flexibility and if it aligns with your goal, you may want to consider the stretch IRA rules and how they can help your IRA assets provide a substantial advantage to your beneficiaries. For example, leaving your IRA assets to a beneficiary with a longer life expectancy may allow more of your IRA assets to remain in the account with the potential to grow tax-deferred for a longer period of time.

If you aren't sure whether or not your spouse may need the assets in your IRA or other retirement savings plans, consider naming your spouse as primary beneficiary and a child, grandchild, or another individual as contingent beneficiary. This step will give you additional flexibility in planning your legacy strategy. For example:

- If you find out later that your spouse will not need the assets after your death, you can change your primary beneficiary to your child, grandchild, or another individual. This move allows the new primary beneficiary to stretch out distributions over his or her own life expectancy — which is probably longer than your spouse's, thus reducing the amount of each distribution and leaving more assets in the IRA to continue to grow tax-deferred.

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## Who Will You Name?

■ After your death, if your spouse doesn't need the assets, he or she can disclaim them (i.e., refuse to take ownership of the assets). The assets will then go to any other named primary beneficiaries or to the contingent beneficiaries (depending on your designations).

■ If you name more than one primary beneficiary, each beneficiary may move his or her share of the assets, after your death, to an Inherited IRA and begin taking distributions based on his or her own life expectancy. (However, the Inherited IRA must be established by December 31 of the year following the year of your death for your beneficiary to take payments over his or her own life expectancy.)

### If Your Beneficiary Is Your Spouse

A spousal beneficiary has the most options, since a spouse can roll your IRA or other tax-qualified retirement plan assets over to a new or existing IRA in his or her own name and designate new beneficiaries. If your spouse has not yet reached the date by which he or she is required to take distributions from the IRA account (age 70½), the assets can remain in the account with the potential to grow tax-deferred until he or she reaches 70½. If your spouse is several years away from age 70½, naming your spouse as beneficiary may be the best strategy to take advantage of the stretch option.



### Options for Other Beneficiaries

Because of the 2006 Pension Protection Act, non-spouse beneficiaries of 401(k) plans, 403(b) plans, pension plans, profit sharing plans, and other employer-sponsored retirement plans may roll the assets into an Inherited IRA, providing tax relief, flexibility, and more options.

Although persons other than your spouse have more limited distribution choices, they can still extend the life of your retirement plan assets. These beneficiaries may be able to take distributions based on their own life expectancies — stretching out distributions for over 30 or 40 years in some cases.

Here's an example that shows the effect of stretching out the distributions using an Inherited IRA. Say a 36-year-old inherits retirement plan assets worth \$500,000 when his father dies, and let's assume that he chooses to roll the money into an Inherited IRA. This beneficiary can stretch receipt of the money over his lifetime by taking only the required minimum distribution each year (based on his life expectancy).

The first graph on the following page shows the year-by-year Required Minimum Distributions (RMDs), and these distributions increase each year as the individual gets older. The

## Leaving a Legacy

Before anything else, you need to name beneficiaries for your retirement accounts. That may seem like an easy task. Remember, though, it is also one of the most important decisions you will make. Therefore, you should give it the time and attention it deserves.

Without doubt, the most important reason for choosing a beneficiary is to make sure your money goes where you want it to go.

By working with your insurance professional, you can help ensure not only that your assets go to the beneficiaries you want, but also that the assets have the potential to grow tax-deferred for years to come.

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second graph indicates the value of the IRA over time. Notice that in the early years, the account grows at a faster rate than the person's annual withdrawals.

However, the required withdrawals increase each year, and by age 65, they exceed the growth of the IRA. At that point, the balance in the IRA begins to decline from the RMDs that are taken.

Nevertheless, by age 75, the individual in this example has withdrawn \$1,720,512 from the Inherited IRA, and still has over \$900,000 left in the IRA account!

## Other Points to Consider

This is just one example of the legacy you can create for the beneficiaries of your retirement plan assets. Of course, the younger the beneficiary, the more time one has to stretch out distributions and the greater the potential legacy.

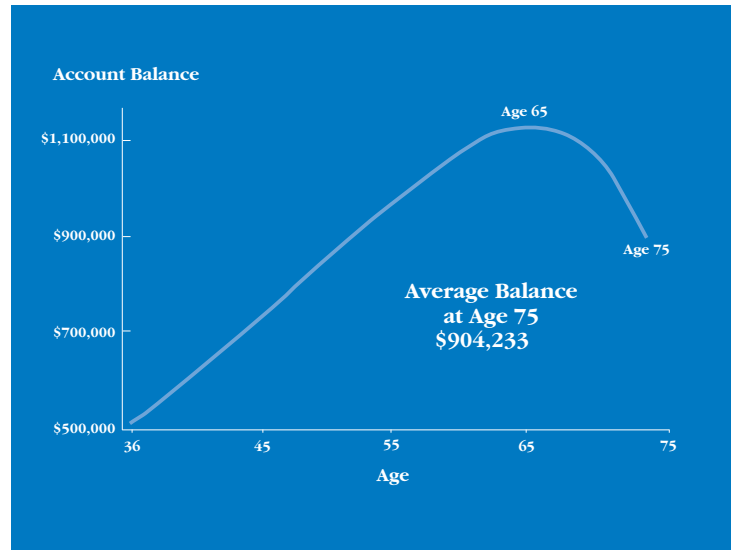
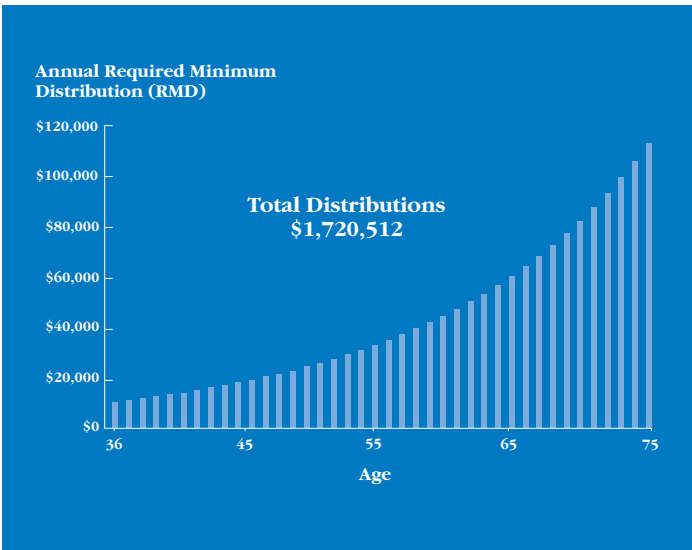
Another issue to consider is your estate tax exemption. Everyone is

currently entitled to a \$2 million exemption from estate taxes.\* If you name a child, grandchild, or other individual, rather than your spouse, as beneficiary on your IRA, you may be able to use your full exemption.\*\*

Remember to let your beneficiaries know that you have named them, since there are deadlines they

must meet in order to take distributions over their life expectancy. Otherwise, in the worst case, they may be forced to take the assets in a lump sum — resulting in a larger tax burden and depriving them of the opportunity to stretch out the assets.

## Benefits of Stretching IRA Assets



In our example, if the recipient is 36 years old it is assumed that the remaining account balance grows at a hypothetical 6% annual rate. This rate is not guaranteed and actual results may be more or less favorable. This example does not illustrate any particular product and does not reflect any charges and fees that may be associated with a particular product.

## Simple Strategies to Make Your IRA Last Longer

Be sure to name both primary and contingent beneficiaries. Naming both provides a clear line of succession in case something happens to your primary beneficiaries. It also provides part of a legacy strategy. After your death, your primary beneficiaries can take distributions, cash out the entire amount, or disclaim the assets altogether. Conversely, failing to name a beneficiary may result in your assets going to your estate, depending on the terms of the IRA. This could have negative tax implications, and may limit your beneficiaries' options.

Remember to let your beneficiaries know that you have named them, since there are deadlines they must meet.

\* Under the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), the estate tax exemption amount is \$2 million for 2007 and 2008, and will increase to \$3.5 million in 2009. In 2010, the estate tax will be repealed for one year. After 2010, the estate tax will be reinstated, and the rates and exemptions in effect pre- EGTRRA will again apply. Under pre-EGTRRA law, the exemption amount after 2010 will be \$1 million.

\*\* Assets passing to surviving spouse generally are not subject to estate taxes at the time of your death due to the Unlimited Marital Deduction. However, if you name your spouse as beneficiary of your IRA and use the Unlimited Marital Deduction, and you do not have enough other assets to pass to your non-spouse beneficiaries, then you may lose some or all of the benefit of your available estate tax exemption.

## Revisit Your Investment Strategy

If your goal for your IRA is to enable your children or grandchildren to receive the IRA assets over their lifetimes, your assets may be invested with the potential to grow tax-deferred for another 40 or 50 years, depending on the ages of the beneficiaries. Therefore, your asset allocation strategy may be different than that of people expecting to use their assets in retirement in the near future.



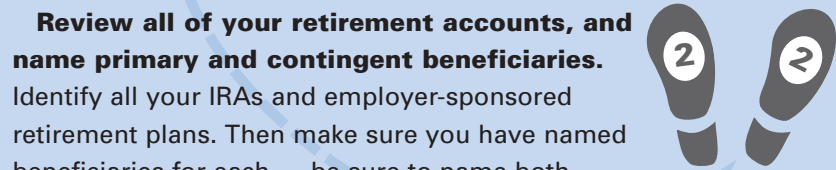
## Where to Start — A Step-by-Step Guide to What You Should Do Now

The following steps can help you organize your thoughts and start you on the path toward successful estate and legacy planning:



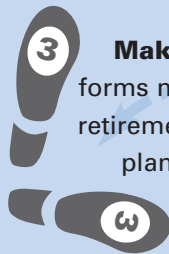
### Identify your retirement needs, goals, and options.

Your financial professional can help you identify all of your retirement plan assets, determine an appropriate way to structure them so you can get the maximum benefit during your lifetime, and help you identify ways to maximize the benefits for your beneficiaries.



### Review all of your retirement accounts, and name primary and contingent beneficiaries.

Identify all your IRAs and employer-sponsored retirement plans. Then make sure you have named beneficiaries for each — be sure to name both primary and contingent beneficiaries.



### Make sure all paperwork is in order.

Beneficiary designation forms must be completed for all IRA and employer-sponsored retirement accounts. Check with your IRA custodian or workplace plan administrator to see whether your beneficiary paperwork is on file. Keep copies with your other estate planning documents so your beneficiaries can find the forms after your death.



**Review documentation regularly.** Review your beneficiary documentation at least once a year. If you've created any new retirement accounts, be certain you've named beneficiaries. Update any beneficiary preferences accordingly.

When you have multiple beneficiaries, each may have different stretch opportunities. If there is a large age difference between your beneficiaries, talk to your insurance professional about how you can help ensure each of them has the ability to stretch out distributions over his or her own life expectancy.



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