



The Practical Aspects of Accepting Beneficiary Designation Gifts

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Charities market beneficiary designations of 401(k)s, IRAs and other qualified plans as an easy, low-cost way to make a tax-wise planned gift. This is true for the most part. The details of completing a beneficiary designation can be more challenging than they appear, however. There are pitfalls and potential mistakes that can result in a failed beneficiary designation and no gift to charity.

How to Make A Gift of a Retirement Plan or IRA

The best way to accomplish a charitable bequest of a retirement plan or IRA is by submitting to the plan administrator a beneficiary designation form for part or all of the retirement plan or IRA. This method, which presents the fewest difficulties and avoids potential pitfalls, simply involves naming of the charity directly as a beneficiary of a death benefit payable under the retirement plan. In such a case, the retirement plan or IRA is paid directly to the charity, not to the donor's estate, and is not governed by the donor's will. By having the benefits paid directly to the charity, neither the estate nor any beneficiary of the estate is subject to income tax attributable to the retirement plan.

In contrast, naming the donor's estate as beneficiary of an IRA and then making a bequest of those assets to charity can subject the estate to potentially adverse income tax consequences. To avoid these adverse income tax consequences the estate must be able to claim an offsetting income tax charitable deduction to eliminate the income tax attributable to the retirement plan or IRA.

Completing the Beneficiary Designation Form

Donors may easily find beneficiary designation forms on their IRA administrator's web site. The donor will usually need to first log in to their account and then look for the "forms" tab. Here are IRA beneficiary designation forms from [Fidelity](#) and [Vanguard](#). The Fidelity form does not specifically mention how to name a charitable beneficiary.

The donor would mark the beneficiary as “other entity” and then enter your charity’s full legal name and tax identification number. The form asks for a date of birth, which the donor should mark as “not applicable.”

The Vanguard form does specifically provide a place to enter a charitable beneficiary. It is concerning though that the Vanguard form only asks for the name of the charity and the percentage of the IRA it is to receive. It is not clear how Vanguard will know which charity is to benefit without a tax ID or at least an address. There are charities with similar names or that have national and local chapters, and charities that have merged.

Take careful note of the disclaimers Fidelity and Vanguard provide on designating a beneficiary of an IRA.

Fidelity: “By signing below, you: ... Agree that Fidelity has no obligation to locate or notify any beneficiary or to independently verify any information submitted by any person claiming an interest in your account.”

Vanguard: “You may designate one or more organizations or charities as beneficiary. Vanguard won't be responsible for contacting any organization or charity after your death nor monitoring how the assets are used. You may want to notify the organization now or advise a trusted person to do so after your death. Please provide the proper name for each entity you designate.”

In other words, if your charity is a beneficiary of an IRA, the administrator may assume no obligation to notify your charity after the owner’s death. The donor or a “trusted person” must advise the charity the gift is coming. The administrator also will not monitor whether their customer’s gift designations are followed. Your charity must ensure the donor’s intentions are carried out.

Here are the takeaways for development officers to ensure proper designation of a charity in a donor’s IRA. Provide your charity’s full legal name, address, and tax identification number to use on the beneficiary designation form. Encourage the donor or the donor’s executor or heirs to inform you that the donor has completed a charitable designation of an IRA to your charity.

Designating A Percentage to Charity

Beneficiary designation forms seem to universally require the plan owner to indicate a percentage of the account to be distributed upon the owner’s death. IRA administrators defend this practice since the account balance that will be left at the plan owner’s death is unknown. If charity is to receive a percentage of the plan at death, determining and distributing that amount will be straightforward.

Designating a Specific Dollar Amount to Charity

A problem arises when a plan owner specifies a pecuniary (that is, specific dollar) amount to be distributed to charity at death. What happens if the other beneficiaries are to receive a percentage of the account? Does the stated dollar amount reduce the

percentages to be received by the other beneficiaries?

By naming the donor's estate as beneficiary, the donor's will can provide greater specificity than is available on the IRA administrator's standard beneficiary designation form. However, there are potential adverse tax consequences in naming the donor's estate as death beneficiary with the donor's will directing the executor to pay a specific amount to a charity. Such a designation has been considered in some cases to be a liquidation of the IRA equal to the dollar amount distributed. That would mean the donor's estate would be liable for income tax on that dollar amount. In the case of a carefully drafted estate plan that pays all charitable distributions with assets like the income from an IRA, the estate should be entitled to an offsetting income tax charitable deduction on the donor's final tax return. Such a plan requires the donor to engage competent counsel to get the desired result.

Instead of adding a provision to the will, the donor's lawyer could draft a customized beneficiary designation to provide a specific dollar amount to charity and other instructions that are not available on the standard beneficiary designation form. This approach can avoid tax problems for the donor's estate. However, the plan administrator may not accept customized beneficiary designations or may only do so for preferred accounts with high account balances.

Spousal Consent

Under federal law, spousal consent is not necessary to name an IRA beneficiary. However, spouses may have rights under state law. For example, if you live in a community or marital property state, spousal consent is generally required to name someone other than the spouse as the beneficiary of an IRA. Those states are Alaska, Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin.

401(k), 403(b), and other workplace retirement account beneficiary rules are different from IRA beneficiary rules. A federal law, the Employee Retirement Income Security Act (ERISA), governs most of these workplace retirement accounts. The spouse of an owner of a workplace retirement account is automatically entitled to receive 50 percent of the account on the death of the plan owner, regardless of what the beneficiary designation says. A properly executed spousal waiver is required if the plan owner designates more than 50% of the account to go to charity or other beneficiaries.

A donor's intent to leave IRA or 401(k) assets to charity could be defeated without a spousal waiver in the situations described above. Only the donor, with advice from advisors or the plan administrator, can determine if and when a spousal waiver is required. Beneficiary designation marketing should caution donors that spousal consent may be required in some cases.

Conclusion

The beneficiary designation is touted as the "easy" planned gift, but there are pitfalls that are important to avoid. Provide as much guidance as you can to inform donors how

to make your charity the beneficiary of their retirement accounts and IRAs. This article has not even touched on the obstacles that charities face in claiming and collecting realized gifts from retirement accounts and IRAs. That challenge will be the subject of a future article.

PG Calc's Consulting Department can answer follow-up questions raised by this article. We look forward to hearing from you!