



Beneficiary 101 for Participants

What are the consequences of an incomplete or inaccurate beneficiary form?

If no beneficiary is designated, the 401(k) plan most likely points the money to your “estate” and the assets become subject to probate. Following death, once all documentation has been sent to the Probate Registry, then the Probate officer will process the claim and send a letter of determination to all financial institutions ordering the decedent’s assets go to whom the officer determines is the rightful heir. This process can be as quick as 3-6 weeks but can last years in a contested situation.

Unlike your home and other investments, account values in a 401(k) or other employer-sponsored retirement plan with a beneficiary designation are treated similarly to transfer-upon-death assets. Under 401(k) beneficiary designation rules, that ownership of the 401(k) assets is transferred to the designated beneficiaries upon the death of the individual account owner rather than being divided as stated in your will or determined by a probate court if you don't have a will.

The end result is 401(k) plan assets are most often allowed to pass through to the designated beneficiary without probate, allowing the beneficiaries to avoid the time and expense of that process. The consequence is that if the deceased participant’s intent for those assets have changed, but the beneficiaries have not been updated appropriately, there is little that can be done to counteract the written beneficiary designation. Additionally, if all the designated beneficiaries in the account were never updated, then those assets will be subject to the time and expense of the probate process.

Imagine this situation: a happily married employee in your company, a proud parent of several children with his first wife, dies unexpectedly. His retirement plan beneficiary information reveals that the primary, 100% beneficiary of his 401(k) are his children. This is due primarily to his ignoring the importance of changing the information following a life event, which in this case was his divorce. The second wife, and not his kids, would be the rightful owner of the retirement benefits!

These situations occur more often than you think and can be easily avoided by maintaining an up to date beneficiary form. When you enroll in a company 401(k) retirement plan, you receive a beneficiary form that asks for both the primary and the contingent beneficiary/beneficiaries. If you die with that 401(k) still undesignated, it will end up in probate court—not a good place to leave grieving loved ones.

Participants must name a primary beneficiary and at least one contingent beneficiary (to whom assets will pass if the primary beneficiary has already passed away). Once the assets have become the property of the primary beneficiary, the backup beneficiary loses all claim.

Who inherits an asset like a 401(k) is a momentous decision—and a critical detail often handled once and then forgotten. Realize the importance of those names on the dotted line and remember to inspect them at least once a year. To learn how various beneficiaries and their life situations may affect designation decisions, consult an estate-planning specialist or tax expert.