8 WAYS TO PROTECT YOUR IRA PLANS

Individual retirement accounts are one of the most popular ways Americans save for retirement. Yet many IRA owners make critical mistakes that can needlessly cost them or their heirs money or thwart the owners' plans. Here are eight ways you can ensure that your IRA works as you designed it.

1. Begin your required minimum distributions on time. Regardless of whether you are still working, you must begin taking an annual minimum required distribution from your traditional IRAs (not Roth IRAs) no later than April 1 following the year you turn 70 1/2. If you don't withdraw enough or you don't withdraw it on time, the IRS will penalize you 50 percent of the difference between the amount you took out and the amount you should have taken out.

The IRS has simplified the calculation of the minimum distribution. Furthermore, the law now requires all IRA custodians and qualified plan administrators (such as 401(k) plans) to inform the owner of the upcoming required distribution and to offer to calculate the minimum distribution amount (for only their account). But it's still up to you to take out the money, which you can draw from any or all accounts you own, as long as the total minimum amount is distributed.

2. Don't wait until the last moment. Some IRA owners wait until the April 1 deadline to take out their initial minimum withdrawal. But remember, you'll have to make another withdrawal by December 31 of the same year. Two minimum withdrawals in the same year could bump you into a higher tax bracket and increase your tax liability.

Also, owners of large accounts may actually reduce their tax bite by taking some withdrawals during lower-income tax years well before they turn 70 1/2.

3. Name a human beneficiary. Failure to name a natural (human) beneficiary usually means the assets go to your estate and that will cost your heirs money. That's because if you hadn't already started taking distributions yourself by the time of your death, the IRA assets must be distributed to your estate's heirs within five years of death. Or if you had started, distributions must be paid out to the heirs over what would have been your remaining life expectancy. Either way, this deprives the heirs from "stretching out" the tax-deferred assets over their own lives and creates a bigger tax bite.

4. Name a contingent beneficiary. This allows the primary beneficiary to "disclaim" (reject) the IRA inheritance if he or she doesn't need the money so that it automatically passes to the contingent, who typically is younger and can stretch out the inheritance longer.

5. Name the right beneficiary. Your spouse isn't always the best choice to name as the primary IRA beneficiary. An adult child might be a better choice but usually not a minor child. Or a trust might be the best choice (such as for a minor child), though that's a complicated decision requiring professional guidance. Don't throw in a charity as a beneficiary to an IRA with human beneficiaries, because it forces accelerated distributions to the named heirs.

6. Changing your beneficiary. Don't forget to change, in writing, your beneficiary in the event of a marriage, divorce, birth of a child, death of a beneficiary or similar circumstances.

7. Have the right number of IRAs. For example, if you have a single large IRA but want to bequeath its assets to multiple heirs and a charity or two, consider separate IRAs for the charities and perhaps for each heir (especially if their ages are significantly different). Lumping them into a single IRA accelerates the required minimum distribution rate the heir(s) are required to take each year.

On the other hand, if you have multiple IRAs but not multiple heirs or charities, consolidating them can reduce paperwork and custodial fees, and make it easier to track investments and calculate minimum distributions.

8. Check to see what your IRA custodian allows. Just because federal law allows you to choose certain options with your IRA doesn't mean the IRA custodian does. The custodian might not allow you to stretch out the payments with your children or grandchildren, for example, or allow the descendants of a deceased beneficiary to receive that heir's share if the IRA has other named heirs. The options are spelled out in the custody agreement.

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