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Once Removed: Filling Out Beneficiary Designations and Payable-on-Death Designations

Episode 54 Summary

A key element of any estate plan is the completion of beneficiary designations and payable-on-death designations for assets. These documents may look routine, but they control who receives certain accounts. This episode discusses issues to consider when filling out these designations, and provides some guidance and potential pitfalls.

Transcript:

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Hello and welcome back.

I'm Steve Murphy, a trust and estates attorney with McGuireWoods LLP. And this is Legacy Planning Once Removed my podcast on estate planning, legacy family, property, probate, and everything else on my clients' minds.

So, on this podcast we help people with estate planning, but we like to take a step back and think about the overall legacy—how to frame it, how to build it. And in this episode, we'll talk about those details to make sure it's carried out simply.

And because we think so much about legacy, we have a tagline here.

We like to say: Walk like you leave footprints.

In this episode, we'll walk through a critical but often overlooked estate planning document, beneficiary designation, and payable-on-death designations.

These simple forms can be critical components of your estate plan, but you might not think of them when you think about their estate plan.

So, let's first ask, what are we talking about?

Well, we're talking about accounts or assets that allow you to leave that asset to an individual upon death.

That's called a beneficiary designation, a payable-on-death designation or a transfer-on-death designation that would provide that upon your death it passes directly to that individual or trust.

Some common examples of this might be life insurance, or you would name a beneficiary to receive the death benefit upon your death.

Or a retirement account, where you again would name a beneficiary who would receive the retirement account upon your death.

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Now, likely these assets can't be retitled into your revocable trust during life. I talked about that on the prior episode.

But even if you could otherwise transfer these assets to a revocable trust during life, you might just prefer to leave them in your individual name and have that payable-on-death (or POD) designation upon your death.

An example of that might be a checking account that allows that kind of designation.

So, what are some key terms before we get started?

Well, I've just mentioned one of them.

The beneficiary designation is the form you would fill out to declare who the beneficiary is. And then we talk about the primary beneficiary—that's the individual or trust or entity who is first in line to receive the asset.

And you could actually have several primary beneficiaries, maybe with different dollar amounts or different percentages.

And then next in line, we talk about a contingent beneficiary. A contingent beneficiary would receive the asset or the share if the primary beneficiary doesn't survive or for whatever reason can't take the asset.

I also like to talk about the default beneficiary. That's the beneficiary who would take the asset if there's no beneficiary designated or if all the beneficiaries don't survive or can't take the asset.

That default beneficiary is really important with many accounts or retirement accounts. The default beneficiary might just be listed as the person's estate.

Well, that would trigger probate or other tax issues. It might be listed as the person's heirs under law.

Well, that might be very different than what the individual's estate plan provides.

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So, keep in mind that default beneficiary, and it's a good idea to fill out those beneficiary designations so you can determine who the beneficiaries are.

And remember that beneficiary designation governs upon your death with very limited exceptions.

Upon your death, the asset passes the way you filled out that beneficiary designation, and the will and the revocable trust agreement wouldn't govern.

So again, these documents can be critical to make sure they're coordinated with the estate plan, so the assets pass the way you would intend.

So just like in our last episode on moving assets to the revocable trust, we're going to ask a couple of questions.

The first is: why?

Why would you want to fill out these beneficiary forms?

Well, I just commented, in some cases it might be required in order to make sure it passes in a specific way upon death.

But also, you might have other assets that you want to pass directly to an individual or directly to your revocable trust upon death in a very simple, efficient way while avoiding probate.

And then we ask another question: what's the overall goal?

Again, think back to the estate plan.

Are there certain assets that you would like to pass outright to an individual?

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It might be common that an individual might want life insurance to pass directly to an individual—maybe a surviving spouse, maybe another individual.

It's also very common that an individual might want their retirement benefit to pass directly to an individual or entity. And there's various income tax advantages at play here too.

In many cases, it's more efficient for a retirement account to pass to a surviving spouse outright.

And it also can be more efficient for a retirement account to pass directly to a charity that can save a considerable amount of income tax upon an individual's death or be a more income tax efficient way to fulfill a bequest.

And then lastly, we'll ask that question: what does the revocable trust say? What does your overall estate plan say?

And again, let's make sure that those beneficiary designations are coordinated with the bequests shares and trusts contained in the revocable trust agreement.

So, the next question is just the nuts and bolts. How do you fill out that form?

Well, you would contact the custodian or administrator of that asset or account, and ask them for that beneficiary designation.

Many times, you can actually go online and fill out a form online. And you want to fill out the primary and contingent beneficiaries very specifically, so for individuals, you want to list their full legal names.

You could consider whether you'd want that share to pass in a certain way if that individual predeceases you—maybe it would pass under those terms like per stirpes or per capita.

These are things you could consult with your advisors about as you fill out the form.

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You could also name a trust as the beneficiary of the account and, again, list that trust very specifically.

I often would encourage clients to include the name of the trustee, the name of the trust document, the date of the trust document and the like.

You'd also want to make sure that the percentages and totals are spelled out accurately.

And there might be situations in which an asset is going to pass to a minor. You might want to make sure that that asset can pass to a uniform transfer to minor's account or similar account to avoid some complexity of managing assets for a minor.

And again, make sure all this titling and these beneficiary designations are consistent across your estate plan.

So lastly, what are a couple of red flags or common mistakes?

You know, what could go wrong here?

Well, I've already alluded to a couple of problems here, especially if these beneficiary designations are not properly coordinated with the overall estate plan.

Number one, you could have problems regarding equalization.

Maybe the revocable trust has specific percentages passing to each individual or specific bequests.

Well, if the beneficiary designations have more assets passing directly to an individual, then it might be that individual sort of gets to double dip in the estate plan, gets too much than was intended.

Another problem we see is outdated designations after marriage, divorce, birth, or death.

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So again, reviewing these beneficiary designations regularly, and especially after those critical life events can be important.

You can imagine lots of individuals might have a retirement plan set up by an employer years and years ago that might have named siblings or others as the beneficiary. That individual's life might have changed now; maybe they're married, maybe they have children, but if they pass away, then that beneficiary designation would govern with limited exceptions.

You also think about what happens if that primary beneficiary does not survive.

So, you want to think about those contingent beneficiaries.

Again, the concern might be what if the primary beneficiary passes away and then the assets pass in a way you didn't intend?

And then for some beneficiaries, like special needs beneficiaries, it might be best to have assets passed to them, not outright, but in a special needs or supplemental needs trust.

So that just might be an example of how passing assets outright to an individual might be problematic.

And then some important takeaways for this concept: the beneficiary of an account or asset could be a great thing to include on that death dossier we talked about on episode 50 and in episode 2, where you keep track of assets and ownership, and let's add that other column—the payable-on-death or transfer-on-death beneficiary and contingent beneficiary, if any.

And remember to review those over time just as you review your other estate planning documents to make sure they're all coordinated.

Well, I'm Steve Murphy and this has been Legacy Planning Once Removed my podcast on thoughtful estate planning.

If this episode was of interest to you about making sure your various accounts and documents are coordinated to help keep things simple for you and your loved ones, check with your attorney or other advisors about your own plan.

And until next time: Walk like you leave footprints.