IOWA STATE UNIVERSITY
Center for Agricultural Law and Taxation

Check Those Beneficiary Designations

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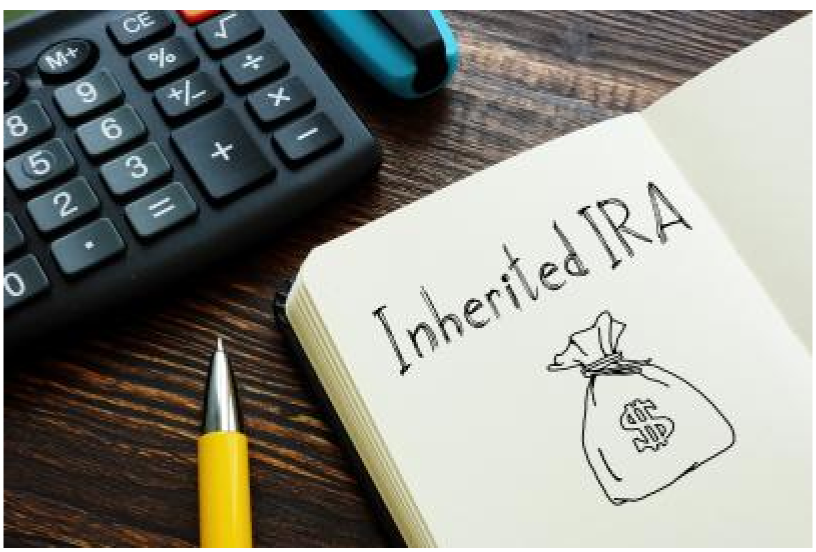
A recent case from the Iowa Supreme Court highlights the importance of carefully completing and reviewing beneficiary designations for IRAs and other retirement accounts. After acknowledging that there was “puzzling language” in the beneficiary designation before it, the Court ultimately determined that it must enforce the agreement based upon what it said, not based upon what the owner may have intended. The case presents a good review of contract interpretation principles and instructs trial courts how to handle extrinsic evidence. It also reminds us to check beneficiary designations for completion and clarity. *U.S. Bank, National Ass’n v. Bittner*, No. 21-0455 (Iowa Sup. Ct. March 3, 2023).



Facts

The owner of the more than $3.5 million IRA at issue was a longtime Iowa attorney who passed away in 2019 at the age of 90. He was survived by his wife and their four children, including a son who was an attorney and the appellant in this case.

2010 Activity

The owner executed a will in 2010. The will provided that his estate would go to a marital trust, to the extent necessary to ensure that no federal estate tax would be paid. The balance was to go to a family trust. The 2010 will also contained language generally stating that the IRA was to be used to provide for his wife during her lifetime and that, upon her death, the IRA was to pass to the family trust. A provision in the will stated that "a substantial part of the income for the benefit of my daughter will be income from my IRA…"

On the same day that he wrote this will, the owner signed a new beneficiary designation for his IRA. This designation took the form of a separate, typed addendum. The form stated at the top that the "Primary Beneficiary" of the IRA was the owner's wife (Joan Y Bittner) and that her share was "100%." Under this designation were several paragraphs of confusing language.

Specifically, the paragraphs repeated that the owner's wife was a primary beneficiary of the IRA, and that she was the primary beneficiary under the marital trust to be created by his 2010 will. It continued, "That part of the IRA necessary to achieve the minimum marital deduction which will result in no federal income tax (sic) is devised to" the marital trust. This addendum then contained a section listing "Contingent Beneficiaries." These included his four children, each named as receiving a 25% share. The document then specified that at the death of the owner's wife, his children were to become the primary beneficiaries of the IRA. Separate from the addendum, the owner checked a box next to "Successor Beneficiaries." This section said that it was not applicable if a trust or estate was the beneficiary. The beneficiary designation did not mention the family trust.

2014 Updates

In 2014, the owner executed a new will, revoking his 2010 will. This will provided for an equal division of his assets between the marital trust and the family trust. It also contained another complex paragraph explaining his wish that the IRA be included in the marital trust, to the extent necessary to result in no federal tax. Unlike the 2010 will, however, the new provision did not mention the family trust, but instead said that the balance of the IRA, at the death of his wife, was to pass as set forth in the beneficiary designation of the IRA. The will continued to state that "a substantial part of the income for the benefit" of his daughter was to be income from his IRA.

The decedent did not update his IRA beneficiary designation in 2014 or in 2017 when he executed an updated IRA agreement.

Confusion at Death

At the death of the owner, the 2014 will was admitted to probate, and the bank serving as the trustee of the IRA asked the court to decide the proper beneficiaries of the IRA. Relying on the designation in the addendum listing the owner's wife as the "Primary Beneficiary" with a "100% share," the bank took the position that the entire IRA should be transferred entirely to her. The wife's conservator and three of the owner's children agreed. The owner's son, however, objected to this transfer. He argued that the IRA should be transferred to the family trust. The district court and the appellate court ruled against the son, and the case came before the Supreme Court.

Supreme Court Explains Contract Interpretation

The Supreme Court took this opportunity to review key contract interpretation rules. First, the Court explained that an IRA, as a trust created for the exclusive benefit of an individual or his beneficiaries, is a form of contract. Consequently, contract principles apply to determine the meaning and legal effect of an IRA beneficiary designation. The Court also affirmed that the IRA agreement, not the will, controls the identity of the designated beneficiary of an IRA agreement.

The Court next explained that contract interpretation involves "bridging" two seemingly incompatible parol-evidence rules (Parol evidence is evidence outside of the four walls of a contract.):

1. Parol evidence is admissible to establish the meaning of a contract.
2. Parol evidence is inadmissible to contradict (or in some cases supplement) a term of a contract.

The Court clarified that these rules mean that no determination of meaning or ambiguity shall be made by a trial court without first considering (1) the contract as a whole and (2) any extrinsic evidence offered by the parties as to the contract's meaning. If at this point the meaning of the contract is unambiguous, parol evidence may not be presented to the fact finder to contradict the terms. Extrinsic evidence cannot change the plain meaning of a writing, but meaning can almost never be plain except in a context.

The Court synthesized these rules into a specific directive for trial judges:

- **Don't keep the evidence out until you've looked at it. Once you've looked at it, if the term is unambiguous, don't allow the evidence to come in for the purpose of contradicting that term.**

The Court continued by summarizing several other key rules:

- The words of the agreement are still the most important evidence of the party's intention.
- Every word and every provision should be interpreted to give it effect, if possible, and an interpretation which gives a reasonable, lawful, and effective meaning to all terms is preferred to one that leaves a part unreasonable, unlawful, or of no effect.
- Courts should assume that no part of an agreement is superfluous.
- Instruments relating to the same transaction which are contemporaneously executed should be construed together.

Interpreting the Contract

The Court then shifted to interpreting the text of the IRA agreement, including the beneficiary designation. As described above, the addendum specifically named the owner's wife as the "primary beneficiary" with a "100%" share. The children were named as successor beneficiaries, and the form stated that the successor beneficiary designation was not applicable if a trust was the beneficiary. Although that portion of the addendum seemed clear, further sections muddied the waters. Several sentences referred to the marital trust, all children were listed as contingent beneficiaries, and the children were supposed to become the primary beneficiaries upon the death of the owner's wife.

The Court reasoned that because the owner's estate did not exceed the threshold for federal estate tax, the marital trust was not funded. Consequently, the statements about the marital trust could be true even if the wife was the 100% beneficiary. Even so—as the son argued—this interpretation rendered many provisions in the addendum superfluous. In response, the Court noted, "The rule against superfluous language is not "the be-all and end-all." It is but one rule of construction.

The Court then considered the son's request to interpret the contract in light of other evidence, such as the wills and prior beneficiary designations. The Court conceded that the trial court should not have shut the door to extrinsic evidence without first examining it. Extrinsic evidence can be helpful to the extent it "sheds light on the situation of the parties…the attendant circumstances, and the objects they were striving to attain." The extrinsic evidence, however, "cannot be used to vary the express terms of the agreement."

Here, the extrinsic evidence did not render the beneficiary designation ambiguous. The Court ruled that the beneficiary provision transferring the IRA was unambiguous and that the wife was to receive the IRA. The decedent may have intended something different, but he didn't achieve that end. The Court said it was significant that the son did not seek reformation based upon a mistake. He did not argue that the owner made an inadvertent error. Instead, he boldly argued that the family trust was the actual designated beneficiary of the IRA, a contention the contract did not support.

Conclusion

This case illustrates how easy it is to make mistakes when completing a rather simple task: filling out a beneficiary designation. In this instance, it appears the owner was trying to do too much and simply failed to pay close attention to the details. As a result, the owner's wishes may have been thwarted. At the very least, resources were wasted on litigation. Judges must play by the rules. They cannot reform unambiguous provisions. As the Court concluded, "Civil litigation is not a quest for perfection. Often judges and juries must deal with a messy situation and decide what outcome, under the law and evidence, makes the most sense—even if it doesn't make perfect sense." Let this be a reminder to check beneficiary designations for clarity, those for IRAs, as well as other retirement accounts and life insurance policies.