

RMD Rules Change Courtesy of the SECURE Act

Effective January 1, 2020, the rules for required minimum distributions (RMDs) and beneficiary payouts have significant changes. Some good; some bad. The changes impact the requirements of both employer retirement plans and IRAs to distribute assets from the plan upon a certain age and upon death.

RMD Rules

Until now, a participant in a retirement plan, or an owner of a Traditional or SIMPLE IRA, was required to start taking minimum distributions each calendar year beginning for the year they reached the magical age of 70½. The SECURE Act, passed in 2019, changes the age RMDs must begin. Beginning in 2020, those who turn age 72 must begin taking RMDs. Participants who started RMDs in an earlier year will continue to take their RMD each year.

The deadline to take the first year's RMD has not changed. A participant's first RMD must be taken by the participant's required beginning date, which is still April 1 following the calendar year they meet the age requirement. Therefore, for those who turn 72 in 2020, their first RMD is required to be distributed by April 1, 2021. Each year thereafter, the RMD is due by December 31. Those who turned age 70½ in 2019, or an earlier year, are not affected by this change—they must continue to take a minimum distribution each year.

For some, this change will delay the start date for RMDs by one year, and for others the delay will be two years. Those who turn 70½ in the first half of 2020 will turn 72 in 2021 and therefore must take their first RMD by April 1, 2022, rather than April 1, 2021. But those who will turn 70½ in the last half of 2020 will not turn 72 until 2022 so their first RMD is now due April 1, 2023—a full two years after it would have been due under the old rules. Just how significant this change is will depend on each individual's own balance and tax situation.

Keep in mind that, although the first RMD for a participant is not due until April 1 of the year following the year in which he attains age 72, it can be taken in the year he turns 72 instead. Waiting to take the first RMD in the following year will mean a requirement to take two years' worth of RMDs in one year. For example, if Joe turns 72 in 2021 and he has an RMD of \$12,000, he can take the \$12,000 distribution in 2021 or by April 1, 2022. His second RMD will be due December 31, 2022 either way. Let's assume his 2022 RMD will be \$13,000. So, Joe can distribute \$12,000 in 2021 and \$13,000 in 2022 or he can take all \$25,000 in 2022 (in actuality, if Joe takes his first RMD in 2021, his 2022 RMD amount will change due to a smaller balance in the plan at the end of 2021). Which option is better for Joe? A distribution is taxable in the year it is taken, so it is up to him (and maybe his tax advisor) to determine the best option.

The examples above apply to "account balance" type benefits, like 401(k) plans and IRAs. Defined benefit plans have different rules. In these plans, the participant must make an election with respect to their entire benefit as of their required beginning date to either commence the annuity or take a total lump sum distribution.

Rules for Beneficiary Payouts

The SECURE Act also changed the rules for required distributions for beneficiaries of retirement plans and IRAs. Until now, if you inherited a retirement plan account you could generally maintain an inherited IRA account and take distributions over your entire life expectancy—and *your* beneficiary could continue to

take this stream of payments. This was often known as a “stretch IRA” and it is going away for many beneficiaries.

Beginning in 2020, if you inherit a retirement account from someone other than your spouse, you will generally be required to deplete the account within 10 years of the year of their death. There will no longer be a requirement to take a minimum distribution each year—just deplete the entire account by the end of the year containing the 10th anniversary of death.

There are exceptions for “eligible designated beneficiaries.” This includes children named as beneficiaries who are minors (as defined under state law), those who are disabled or chronically ill, and beneficiaries who are no more than 10 years younger than the decedent (e.g., siblings, friends). However, once these eligible designated beneficiaries pass away, *their* beneficiaries must distribute the account balance within 10 years. Also, once a minor child reaches the age of majority under state law, they will have 10 years to deplete the account. A spouse beneficiary can continue to treat the account as their own without regard to the new rules.

The new rules apply to accounts of those who die on or after January 1, 2020. Anyone who inherited an account due to a death before this date can continue to take advantage of the old rules, but upon their death, their beneficiary will have just 10 years to deplete the account (they cannot continue to use the first beneficiary’s life expectancy).

The new rules will have a significant impact on the estate planning for individuals with large retirement account balances. Unless their beneficiary is their spouse, the options to stretch out this benefit over many years, and their tax planning options, will be much more limited.