PROPOSED RMD REGULATIONS: A SURPRISE FOR SOME DESIGNATED BENEFICIARIES

The proposed final regulations have been released for post-death distributions from qualified accounts after the Setting Every Community Up for Retirement Enhancement (SECURE) Act. Proposed does not mean final, but there are areas in which designated beneficiaries (DBs), or potential DBs, may want to plan.

The SECURE Act changed the post-death required minimum distribution (RMD) rules for qualified accounts. The new proposed final RMD regulations clarify some areas and provide needed details in others. The IRS released the proposed final RMD regulations for comments, which were due 5/25/22. The public hearing was held on 6/15/22, and it is reasonable to expect the regulations to be finalized this year.

The proposed regulations are extensive. This blog will focus on distributions after death from a qualified account in which the beneficiary is a designated beneficiary (DB). Other blogs discuss spousal and other eligible designated beneficiary (EDB) options as well as a trust as the beneficiary of an Individual Retirement Account (IRA).

Generally, changes in planning are best made when regulations are final. But for some DBs, planning now may allow for better choices later.

When Might the Proposed Regulations Go into Effect?

The proposed regulations would go into effect for calendar years beginning on or after 1/1/22. Yes, that means that the regulations could apply to actions taken in 2022. For this reason, there are some actions that might be put on hold–or taken–now.

What Do the Proposed Final Post-Death RMD Regulations Clarify?

The proposed regulations clarify how the SECURE Act post-death 10-year rule applies, including a surprising interpretation of post-required beginning date (RBD) rules. As this is a complicated area, let's consider the hypothetical situation below to better understand how different DBs could be affected.

As the result of a tragic accident in 2022, Sam's parents, Diane, age 71, died on a Monday, and Derrick, age 73, died the next day. Derrick named Sam as the beneficiary of his IRA at the investment firm, but never completed the beneficiary form for his IRA account at the bank. Diane named Sam as the beneficiary of her IRA. Sam is also the sole beneficiary of each parent's estate.

Under the current interpretation of the 10-year rule, the outcome is easy to determine: Sam must deplete the accounts where he is named a beneficiary by 12/31 of the year containing the 10th anniversary of his parents' deaths. He is not required to take distributions prior to the final date.

The question: What options will Sam, age 38, a DB, have for distributions under the proposed rules? The answer is tricky.

After the Proposed Regulations

Beneficiary	Derrick's IRA–Investment House	Diane's IRA	Derrick's IRA–Bank
Sam	Derrick had passed his RBD and had started RMDs. Under the proposed regulations, Sam must take RMDs in years 1 to 9. The account must be fully distributed by December 31 of the year containing the 10th anniversary of Derrick's death.	Diane had not yet reached her RBD. Nothing changes for Sam. He does not have to take distributions for years 1 through 9, but must fully distribute the account by December 31 of the year containing the 10th anniversary of Diane's death.	Not applicable.
Derrick's Estate	Not applicable.	Not applicable.	Derrick did not name a beneficiary, but the bank IRA custodial agreement does: first, to the surviving spouse, then to the estate. As Derrick did not have a surviving spouse, the beneficiary is his estate. Derrick's estate is not a DB, so it can use his "ghost" life expectancy based on IRS Table I (Single Life) of 14.8 years (same as prior to proposed regulations).

What, if Any, Steps Should Clients Take Today?

For many clients who are DBs, distributions will occur as expected. But some client DBs may need to prepare for changes.

- **DB where the IRA account owner died BEFORE 1/1/20.** If these DB clients elected to stretch, nothing changes. They continue their fixed life expectancy distributions. As before, successor beneficiaries generally must follow the 10-year rule, so additional planning may be required.
- **DB where the IRA account owner died 1/1/20 or later and BEFORE the RBD.** These clients follow the 10-year rule as understood before the regulations were published. No distributions are required in years 1 to 9. The account must be fully distributed in the year containing the 10th anniversary of the account owner's death.
- **DB where the IRA account owner died 1/1/20 or later and AFTER the RBD. *These clients may need to take action.*** There are several items to consider:
  - **Potential distributions for 2022.** The regulations are not final. Unless funds are needed, it may make sense to postpone taking the 2022 distribution until later this year. It also may make sense to consider ways to reduce income going forward, such as using a variable annuity to help time and control the recognition of gains.
  - **Potential "catch-up" requirements for 2021.** The IRS has not clarified if a "catch-up" distribution is required for 2021. This means a DB could have TWO distributions in 2022. Some clients may want to determine if additional planning, such as deferring other income, will help manage their brackets.

- **DBs who planned on 10 years without distributions.** Some clients may plan to have distributions in the 10-year period match a specific event or date. As an example, a client DB targeting retirement in five years might have planned to avoid taking distributions while still working. This may no longer be an option.

This is also the perfect time to review beneficiary designations and determine if the proposed final RMD regulations affect client goals for the transfer of these assets. Adjustments may be required.

The proposed final RMD regulations are likely to keep most provisions. Clients may want to plan now to allow for more flexibility. Reaching out to clients today may give them more options in the future!

Additional Resources and Links

Required Minimum Distributions (Federal Register)

The SECURE Act: Several Key Retirement Plan Provisions

Further Consolidated Appropriations Act of 2020 (includes SECURE Act)

For more information about retirement planning, please contact our Retirement Strategies Group at RSG@PacificLife.com or (800) 722-2333, ext. 3939.
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