
How to Interpret the Proposed RMD Regs: Wagner Law

By Wagner Law Group Thu, Apr 14, 2022

Without special 'see-through' trust provisions, a retirement asset with a trust as beneficiary may need to be distributed by the end of the 5th year following the year the participant dies, writes Wagner Law Group attorney Barry Salkin. He clarifies the proposed RMD regs.

The SECURE Act (the “Act”) made two major changes to the required minimum distribution rules under Internal Revenue Code (“Code”) Section 401(a)(9):

1. It extended the required beginning date for distributions from age 70-1/2 to age 72, other than distributions from tax-qualified plans which can be deferred until retirement except in the case of 5% owners, and
2. Except for a limited category of beneficiaries, it substantially reduced the period over which post-death distributions can be made, the latter element of which is sometimes referred to as eliminating the stretch IRA.

The IRS recently issued proposed regulations implementing these statutory changes, which apply to tax-qualified retirement plans, 403(b) plans, IRAs, and eligible deferred compensation plans under Code Section 457.

Compliance with the proposed regulations constitutes a reasonable, good faith interpretation of the amendments made by the SECURE Act. The proposed regulations would apply for purposes of determining required minimum distributions for calendar years beginning on or after January 1, 2022. For a 2021 calendar year distribution paid in 2022, taxpayers must apply the existing Code Section 401(a)(9) regulations.

The proposed regulations address the effective date for both of the SECURE Act statutory modifications. With respect to the new required beginning date of age 72, the SECURE Act provided that this change applied to individuals who attain age 72 on or after January 1, 2020. The statutory language could have been read as providing that if the individual died prior to January 1, 2020 and before attaining age 70-1/2, then the existing rule would apply. However, IRS took the position that the new rule should apply to any individual who would have attained age 72 on or after January 1, 2022 had he or she survived, which includes those born on or after July 1, 1949.

With respect to the new distribution rules, the relevant date for determining which set of

regulations should apply to a trust providing for multiple beneficiaries depends upon the date of death of the oldest beneficiary.

As amended, Code Section 401(a)(9) retains the existing distribution periods for five (5) categories of beneficiaries, referred to as “eligible designated beneficiaries” or “EDBs”—surviving spouses, minor children of the individual, disabled persons, chronically ill persons, and beneficiaries who are not more than 10 years younger than the individual. With respect to this latter requirement, the proposed regulations take the position that there must actually be a 10-year age difference between the participant and the beneficiary. These EDBs can continue to receive payments based on life expectancy payments and are not required to receive the balance after 10 years.

For designated beneficiaries who are not eligible designated beneficiaries, all distributions must be completed by the end of the tenth year following the date of the death of the plan participant or the owner of an IRA. If the individual had already begun receiving payments, payments must continue to the designated beneficiary based on the designated beneficiary’s life expectancy, but if the individual had not already begun receiving payments, i.e., the individual died before his required beginning date, the designated beneficiary can defer all distributions until the end of the tenth year following the date of death of the plan participant or the owner of an IRA.

From the perspective of a defined contribution plan sponsor, the proposed regulations provide that, if the employee has an eligible designated beneficiary, the plan may provide either that the life expectancy rule applies or the 10-year rule applies. Alternatively, the plan may provide the employee or EDB with an election between the 10-year rule and the life expectancy rule. However, if the defined contribution plan does not include either of these options, the default option is the life expectancy rule. As a result, it is first necessary to determine which individuals qualify as eligible designated beneficiaries, and the proposed regulations provided this additional guidance:

1. Children. For defined contribution plans, the age of majority for a child is age 21, the age of majority in most jurisdictions (a few jurisdictions have younger ages, but none have older ages). However, defined benefit plans that were applying the definition of age of majority in the existing regulations may continue to do so. The proposed regulations do not define “child,” but as the SECURE Act commentary indicates that the intention was to limit it and certainly to exclude grandchildren, it appears that “child” means biological or adopted children of the participant.

2. Disability. With respect to disability, if the beneficiary is under the age of 18, the definition of disability is modified to be a “medically determinable physical or mental impairment that results in marked and severe functional limits, and can be expected to result in death or be of long-continued and indefinite duration.” A determination of Social Security disability is a safe harbor.

a. Date of Determination. The date of disability is determined as of the employee’s death. As a result, if the beneficiary is a minor child and the child becomes disabled after the date of the employee’s death, the child will cease to be an eligible designated beneficiary when the child attains age 21.

b. Documentation. The documentation requirements for disabled and chronically ill individuals, including the required certifications by licensed health care practitioners, must be provided by October 31 of the calendar year following the calendar year of the employee’s death.

3. Multiple Beneficiaries. Naming more than one designated beneficiary can be especially problematic. If just one of the group is not an eligible designated beneficiary, that preferred status is lost for the entire group. All must be eligible designated beneficiaries, or all must be treated as designated beneficiaries. There are two exceptions to this general rule. An eligible designated beneficiary who is appointed with one or more others who are simply designated beneficiaries may extend distributions over his or her life expectancy if:

a. The eligible designated beneficiary is a child. If the beneficiary is the child of the employee and had not reached the age of majority (age 21) at the time of the employee’s death, then that child will be treated as an eligible designated beneficiary.

b. The eligible designated beneficiary is such because he or she is disabled or chronically ill and is entitled to lifetime benefits in a multi-beneficiary trust which will not pay benefits to others prior to that individual’s death.

Separate accounting rules are applied to the individual interests of the beneficiaries in trusts with multiple beneficiaries.

A variety of issues arise in determining whether an individual is an eligible designated beneficiary, particularly where the nominal beneficiary is a trust. Without special “see-through” trust provisions, a retirement asset with a trust as beneficiary may need to be distributed by the end of the 5th year following the year the participant dies. The proposed regulations provide numerous examples, and the preamble to the proposed regulations

discusses this issue in detail. We encourage all individuals to seek competent tax counsel for their unique situations.

As with most IRS regulations, the regulation package is lengthy - 275 pages. A great deal of guidance is presented in the preamble and the proposed regulations, which is relevant from both an employee benefit perspective and an estate planning perspective. This client alert is the first in a series of client alerts that will discuss different aspects of the proposed regulations.

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