Advanced Markets Matters

RMD Opportunities

A Financial Professional's Guide

RMD Opportunities: Timing is Everything

Help Your Clients Understand RMDs

An understanding of the RMD rules can provide opportunities to help clients manage and plan their RMDs — opportunities to regulate, minimize and delay.

Strategies for Managing and Planning RMDs

RMDs (Required Minimum Distributions) are neither inherently good nor bad. They are simply a consequence of having benefited from tax deferral and tax exclusion or tax deductibility while saving for retirement. The government accordingly wants those tax-advantaged retirement dollars to actually be used for retirement. It just makes sense. Thus, distributions must generally begin by a certain age or time and cannot be stretched out too long.

Rules to Remember

Distributions from qualified plans and traditional IRAs must generally begin at age 70½ or, if earlier, death. Distributions from Roth IRAs must begin upon the death of the owner.

50% Penalty for Missing an RMD

The penalty for failing to take an IRS-mandated distribution is 50 percent of the shortfall (the amount that was mandated to be withdrawn but was not). That's one of the highest penalties imposed by the IRS outside of fraud or abuse cases.

Distributions in Detail

Distributions: During Lifetime

Who?

Traditional IRA owners and qualified plan participants.[1]

When?

Must begin by the individual's required beginning date (RBD).

Traditional IRA Owner	April 1 of the year following the year the individual turns 70½
Plan Participant/More-than-5-percent Owner	April 1 of the year following the year the individual turns 70½
Plan Participant/**Not** More-than 5-percent Owner	April 1 of the year following the later of the year the individual turns 70½ or retires

Delay?

Qualified plan participants who own 5 percent or less of the business and plan on working past age 70½ can delay their RMDs — provided the plan allows deferrals beyond that age. **Note: The delay applies only to the qualified plan of the current employer**.

How?

RMDs from IRAs and qualified plans not annuitized are calculated using the **life expectancy method**. Using this method, the amount that must be distributed each year is determined by:

Account Balance as of December 31 of Prior Year ÷ **Life Expectancy Factor**

The life expectancy factor is taken from the Uniform Lifetime Table (see page 6) *unless* the sole beneficiary of the account is the individual's spouse and the spouse is more than 10 years younger than the individual. In that case, use the Joint and Last Survivor Table. It will produce larger factors and thus smaller RMDs.

Individuals can delay their RMD for their first distribution year until April 1 of the following year (their required beginning date). However, if individuals do wait until April 1 of the following year, they must take a **second** RMD by December 31 of that same year. For determining the amount of the RMD for the second and future distribution years, the appropriate table is re-entered each year using the age of the individual as of the end of that calendar year (the "attained age" method).

1 RMD rules for Section 457 and 403(b) participants are beyond the scope of this guide.

Distributions in Detail

Distributions: Upon Death

Who?

Beneficiaries of qualified plan participants and traditional IRA participants, as well as non-spouse beneficiaries of Roth IRAs.

Designated beneficiaries may be permitted to stretch payments over their life or life expectancies. Generally, a designated beneficiary is any individual designated as a beneficiary of the IRA. A charity or an estate cannot be considered a designated beneficiary; therefore, distributions may not be stretched. A trust may be a permitted designated beneficiary if the trust meets certain requirements.

Designated beneficiaries are determined as of September 30 of the year after the year of the individual's death. Any non-individual beneficiaries may be paid out before this deadline to retain stretch opportunities for any remaining designated beneficiaries.

When?

If the individual *dies before their RBD*, the entire account must be distributed by December 31 of the year that contains the fifth anniversary of the individual's death, unless they have a designated beneficiary. Distributions to a designated beneficiary may be stretched over the life expectancy of the designated beneficiary as long as the distributions begin no later than December 31 of the year after the year of the individual's death.[2]

If the individual *dies on or after their RBD*, RMD regulations allow the account balance to be distributed over the longer of the life expectancy of the designated beneficiary or the life expectancy of the individual.

How?

For non-spouse beneficiaries, the age of the designated beneficiary as of December 31 of the year after the death of the individual is entered into the Single Life Table to determine the appropriate factor to be used to calculate the RMD for that first year. Thereafter, one (1) is subtracted from that original factor each year to determine the RMD (the reduction method).

Example: Bill died in 2018 at age 69. His son Jon was his designated beneficiary on his IRA. He turned 45 in 2019. Thus, Jon's RMD for 2019 was determined by dividing the account balance in the IRA as of December 31, 2018, by the single life factor of 38.8 for a 45-year-old. The RMD for 2020 would be determined by dividing the IRA's account balance as of December 31, 2019, by 37.8 (38.8 - 1).

If multiple individuals are named as designated beneficiaries, the age of the oldest is used to calculate RMDs. If an IRA with multiple individual designated beneficiaries is split into separate accounts by December 31 of the year after the year of death, then the life expectancy of the oldest beneficiary on each account is used.

2 While distributions do not need to begin until December 31 of the year following the year of death, the election to stretch the payments needs to be made within 60 days of the date of death.

Added Considerations

Special Rules for Surviving Spouses

1. Any surviving spouse who is a designated beneficiary may elect to rollover the decedent's IRA or plan account into their own IRA or plan account.

2. A surviving spouse who is the sole designated beneficiary of the decedent's IRA may elect to treat the decedent's IRA as their own.

3. In the case of the decedent dying before their RBD, the surviving spouse who is the sole beneficiary may delay taking RMDs from the inherited IRA or plan account until the deceased spouse would have turned age 70½.

4. If the surviving spouse is the sole beneficiary and holds the decedent's IRA or plan account as an inherited plan, the surviving spouse uses the attained age method and re-enters the Single Life Table each year.

5. Spousal beneficiaries of Roth IRAs who rollover or treat the decedent's Roth IRA as their own are not required to take RMDs during their lifetime.

Remember: Aggregation Rules Differ

Qualified Plans: RMDs must be calculated **for** each separate qualified plan and distributed **from** each separate plan.

Traditional IRAs: RMDs must also be calculated separately for each IRA; however, an individual generally may total the amount of RMDs from each IRA but then take the total amount from one or more IRAs.

Exceptions:

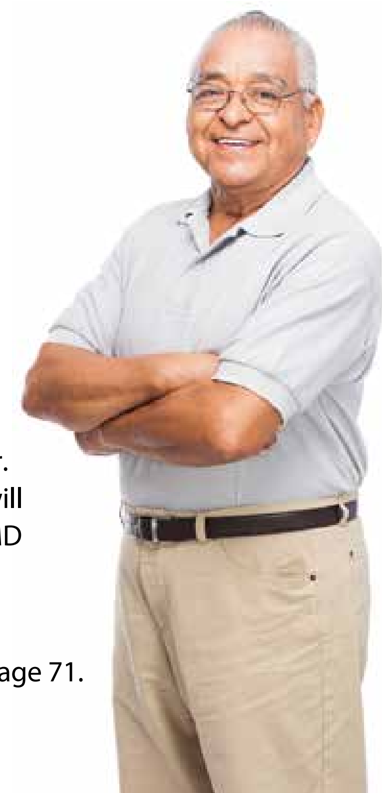
- IRAs held as an owner cannot be aggregated with IRAs held as a beneficiary
- IRAs held as a beneficiary can be aggregated with other IRAs inherited from the same decedent only

Planning Point: No Rollovers for Non-Spouse Beneficiaries

A non-spouse beneficiary of a qualified plan or IRA is prohibited from rolling over an inherited account into their own name. They may, however, do a trustee-to-trustee transfer of such funds to an inherited IRA account that is titled as such – in the name of the decedent for the benefit of the beneficiary. RMDs must continue to be taken from the new inherited account.

Case Study

Stu Takes Two: Traditional IRA Owner



First distribution year: Stu turned 70 in March of 2018. That made 2018 his first distribution year. He is not married to a spouse who is more than 10 years younger.

1. Stu enters the Uniform Lifetime table using his age as of December 31 of the distribution year – age 70. The factor is 27.4.
2. Stu divides his account balance as of December 31, 2017 – $274,000 – by 27.4. His RMD for 2018 is $10,000, whether he takes the distribution in 2018 or delays until April 1 of the following year. The factor and account balance does not change.

Second distribution year: The amount of the RMD for Stu's second distribution year – 2019 – will vary depending on whether he delayed his RMD for the first distribution year. His factor will be the same — he re-enters the table at age 71. But his account balance will be smaller if he takes his 2018 RMD in 2018 rather than if he waits and takes his 2018 RMD in 2019.

Insight: If Stu turned 70 in August instead of March, he would have turned 70½ in 2019. That would make 2019 his first distribution. He would have entered the table in 2019 at age 71.

Uniform Lifetime Table with Percentages

Taxpayer's Age	Life Expectancy Factor	Percentage	Taxpayer's Age	Life Expectancy Factor	Percentage
70	27.4	3.65%	93	9.6	10.42%
71	26.5	3.77%	94	9.1	10.99%
72	25.6	3.91%	95	8.6	11.63%
73	24.7	4.05%	96	8.1	12.35%
74	23.8	4.20%	97	7.6	13.16%
75	22.9	4.37%	98	7.1	14.08%
76	22.0	4.55%	99	6.7	14.93%
77	21.2	4.72%	100	6.3	15.87%
78	20.3	4.93%	101	5.9	16.95%
79	19.5	5.13%	102	5.5	18.18%
80	18.7	5.35%	103	5.2	19.23%
81	17.9	5.59%	104	4.9	20.41%
82	17.1	5.85%	105	4.5	22.22%
83	16.3	6.13%	106	4.2	23.81%
84	15.5	6.45%	107	3.9	25.64%
85	14.8	6.76%	108	3.7	27.03%
86	14.1	7.09%	109	3.4	29.41%
87	13.4	7.46%	110	3.1	32.26%
88	12.7	7.87%	111	2.9	34.48%
89	12.0	8.33%	112	2.6	38.46%
90	11.4	8.77%	113	2.4	41.67%
91	10.8	9.26%	114	2.1	47.62%
92	10.2	9.80%	115+	1.9	52.63%

Strategies and Takeaways

R

Regulate

RMD rules are complex. The 50% penalty for not complying is significant. Clients can regulate their RMDs, that is, "bring order, method, or uniformity" to their RMDs with a "fix it and forget it" strategy utilizing the automatic payouts of a single premium immediate annuity (SPIA).

Fix It and Forget It With a SPIA

Different rules apply to funds in IRAs and defined contribution plans that are annuitized. The IRS generally considers the purchase of a SPIA to satisfy RMD obligations if the annuity is not payable over a period extending beyond the life expectancy of the IRA owner (and, if applicable, designated beneficiary) and meets certain other requirements.

Annual calculations are not required. However, the annuity payout will only satisfy the RMD rules for the funds in the IRA annuity. The income payouts cannot be used to satisfy RMDs for non-annuitized IRA funds in any year other than the year of the transfer.

M

Minimize

RMDs can be minimized by converting pre-tax amounts in traditional IRAs to Roth IRAs **to the extent it can be done at lower rates**. With income tax rates set to increase after 2025, a series of partial conversions (staying within current tax brackets) by pre-retirees can reduce the balance in their traditional IRAs and thus reduce their RMDs in future years.

Income Tax Rates Reduced for Now

Roth IRAs may make even more sense now after tax reform. With income taxes temporarily reduced, it may make sense to contribute directly to Roth IRAs. It may even make sense for IRA owners to convert amounts in traditional IRAs to the extent they can do so in lower brackets. IRA owners who expect that they and their beneficiaries will always be in a very high tax bracket may want to convert their entire IRA as quickly as they can.

Its important to consider the effect of any conversion and increased adjusted gross income on applicable capital gains tax rates, Social Security benefits taxation and Medicare premiums.

D

Delay

Contributing to Roth IRAs and converting traditional IRAs into Roth IRAs can delay RMDs until after the death of the IRA owner. Designated Roth accounts [401(k) and 403(b)] are subject to RMD rules during lifetime. Rolling those amounts into Roth IRAs delays the need for RMDs until after the death of the Roth IRA owner.

Tax-Deferred And Tax-Free

Roth IRAs are funded with after-tax contributions and qualified distributions (including earnings) from Roth IRAs are not subject to income taxation. Thus, the IRS has already received its money and has no reason to require distributions during the Roth IRA owner's or spouse's lifetime.

For those who may not need to withdraw funds from their Roth IRA for retirement living expenses, a Roth IRA may provide a significant opportunity to pass on a growing inheritance to named beneficiaries.

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