



Required minimum distributions

WHAT ARE REQUIRED MINIMUM DISTRIBUTIONS (RMDs)?

Required minimum distributions, often referred to as RMDs or minimum required distributions, are amounts that the federal government requires you to withdraw annually from traditional IRAs and employer-sponsored retirement plans after you reach age 72 (if you attain age 70 1/2 after 2019) or, in some cases, after you retire. You can always withdraw more than the minimum amount from your IRA or plan in any year, but if you withdraw less than the required minimum, you will be subject to a federal penalty.

The RMD rules are designed to spread out the distribution of your entire interest in an IRA or plan account over your lifetime. The purpose of the RMD rules is to ensure that people don't just accumulate retirement accounts, defer taxation and leave these retirement funds as an inheritance. Instead, RMDs generally have the effect of producing taxable income during your lifetime.

WHICH RETIREMENT SAVINGS VEHICLES ARE SUBJECT TO THE RMD RULES?

In addition to traditional IRAs, Savings Incentive Match Plan IRAs and Simplified Employee Pension IRAs are subject to the RMD rules. Roth IRAs, however, are not subject to these rules

while you are alive. Although you are not required to take any distributions from your Roth IRAs during your lifetime, your beneficiary will generally be required to take distributions from the Roth IRA after your death.

Employer-sponsored retirement plans that are subject to the RMD rules include qualified pension plans, qualified stock bonus plans and qualified profit-sharing plans, including 401(k) plans. Section 457(b) plans and Section 403(b) plans are also subject to these rules. If you are uncertain whether the RMD rules apply to your employer-sponsored plan, you should consult your plan administrator or a tax professional.

WHEN MUST RMDs BE TAKEN?

Your first required distribution from an IRA or retirement plan is for the year you reach age 72 (if you attain age 70 1/2 after 2019). However, you have some flexibility as to when you actually have to take this first-year distribution. You can take it during the year you reach age 72 (if you attain age 70 1/2 after 2019), or you can delay it until April 1 of the following year.

Note: If you reach age 72 before July 1, 2022, you will need to take an RMD by December 31, 2022.

Since this first distribution generally must be taken no later than April 1 following the year you reach age 72 (if you

attain age 70 1/2 after 2019), this April 1 date is known as your required beginning date. Required distributions for subsequent years must be taken no later than December 31 of each calendar year until you die or your balance is reduced to zero. This means that if you opt to delay your first distribution until April 1 of the following year, you will be required to take two distributions during that year – your first year’s required distribution and your second year’s required distribution.

Example: *You have a traditional IRA. Your 72nd birthday is December 2, 2022. You can take your first RMD during 2022, or you can delay it until April 1, 2023. If you choose to delay your first distribution until 2023, you will have to take two required distributions during 2023 – one for 2022 and one for 2023. This is because your required distribution for 2023 cannot be delayed until the following year.*

There is one situation in which your required beginning date can be later than described above. If you continue working past age 70 1/2 (age 72 if you attain age 70 1/2 after 2019) and are still participating in your employer’s retirement plan, your required beginning date under the plan of your current employer can be as late as April 1 following the calendar year in which you retire (if the retirement plan allows this and you own 5% or less of the company). Again, subsequent distributions must be taken no later than December 31 of each calendar year.

Example: *You own more than 5% of your employer’s company and you are still working at the company. Your 72nd birthday is on December 2, 2021. You must take your first RMD from your current employer’s plan by April 1, 2022 – even if you’re still working for the company at that time.*

Example: *You participate in two plans – one with your current employer and one with your former employer. You own less than 5% of each company. Your 72nd birthday is on December 2, 2022, but you’ll keep working until you turn 73 on December 2, 2023. You can delay your first RMD from your current employer’s plan until April 1, 2024 – the April 1 following the calendar year in which you retire. However, as to your former employer’s plan, you must take your first distribution (for 2022) no later than April 1, 2023 – the April 1 after reaching age 72.*

HOW ARE RMDs CALCULATED?

RMDs are calculated by dividing your traditional IRA or retirement plan account balance by a life expectancy factor

found in Publication 590-B (most IRA owners will use the Uniform Life Table). Your account balance is calculated as of December 31 of the preceding year for which the distribution is required to be made.

Example: *You have a traditional IRA. Your 72nd birthday is November 1 of year one and you reach age 72 in year one. Because you turn 72 in year one, you must take an RMD for year one from your IRA. This distribution (your first RMD) must be taken no later than April 1 of year two. In calculating this RMD, you must use the total value of your IRA as of December 31 of year zero.*

Caution: *When calculating the RMD amount for your second distribution year, you base the calculation on the IRA or plan balance as of December 31 of the first distribution year (the year you reached age 72) regardless of whether or not you waited until April 1 of the following year to take your first required distribution.*

For most taxpayers, calculating RMDs is straightforward. For each calendar year, simply divide your account balance as of December 31 of the prior year by your distribution period, determined under the Uniform Lifetime Table using your attained age in that calendar year. This life expectancy table is based on the assumption that you have designated a beneficiary who is exactly 10 years younger than you are. Every IRA owner’s and plan participant’s calculation is based on the same assumption.

There is one exception to the procedure described above. If your sole designated beneficiary is your spouse, and they are more than 10 years younger than you, the calculation of your RMDs may be based on the longer joint and survivor life expectancy of you and your spouse. (These life expectancy factors can be found in IRS Publication 590.) Consequently, if your spouse is your designated beneficiary and is more than 10 years younger than you, you can take your RMDs over a longer payout period than under the Uniform Lifetime Table. If your beneficiary is a nonspouse or a spouse who is not more than 10 years younger than you, you are subject to the shorter payout period under the simplified general rule.

If you have multiple IRAs, an RMD is calculated separately for each IRA. However, you can withdraw the required amount from any one or more IRAs. Inherited IRAs are not included with your own for this purpose. (Similar rules apply to Section

403(b) accounts.) If you participate in more than one employer retirement plan, your RMD is calculated separately for each plan and must be paid from that plan.

SHOULD I DELAY TAKING MY FIRST RMD?

Your first decision is when to take your first RMD. Remember, you have the option of delaying your first distribution until April 1 following the calendar year in which you reach age 72 (or April 1 following the calendar year in which you retire, in some cases).

You might delay taking your first distribution if you expect to be in a lower income tax bracket in the following year, perhaps because you're no longer working or will have less income from other sources. However, if you wait until the following year to take your first distribution, your second distribution must be made on or by December 31 of that same year.

Receiving your first and second RMDs in the same year may not be in your best interest. Since this "double" distribution will increase your taxable income for the year, it will probably cause you to pay more in federal and state income taxes. It could even push you into a higher federal income tax bracket for the year. In addition, the increased income may cause you to lose the benefit of certain tax exemptions and deductions that might otherwise be available to you. So the decision of whether to delay your first required distribution can be important, and should be based on your personal tax situation.

WHAT IF I FAIL TO TAKE RMDs AS REQUIRED?

You can always withdraw more than you are required to from your IRAs and retirement plans. However, if you fail to take at least the RMD for any year (or if you take it too late), you will be subject to a federal penalty. The penalty is a 50% excise tax on the amount by which the RMD exceeds the distributions actually made to you during the taxable year.

Example: You own one traditional IRA and compute your RMD for year one to be \$7,000. You take only \$2,000 as a year-one distribution from the IRA by the date required. Since you are required to take at least \$7,000 as a distribution but have only taken \$2,000, your RMD exceeds the amount of your actual distribution by \$5,000 (\$7,000 minus \$2,000). You are therefore subject to an excise tax of \$2,500 (50% of \$5,000).

Technical note: You report and pay the 50% tax on your federal income tax return for the calendar year in which the distribution

shortfall occurs. You should complete and attach IRS Form 5329, "Additional Taxes on Qualified Plans (Including IRAs) and Other Tax-Favored Accounts." The tax can be waived if you can demonstrate that your failure to take adequate distributions was due to "reasonable error" and that steps have been taken to correct the insufficient distribution. You must file Form 5329 with your individual income tax return and attach a letter of explanation. The IRS will review the information you provide and decide whether to grant your request for a waiver.

TAX CONSIDERATIONS

ARE RMDs SUBJECT TO INCOME TAX?

Like all distributions from traditional IRAs and retirement plans, RMDs are generally subject to federal (and possibly state) income tax for the year in which you receive the distribution. However, a portion of the funds distributed to you may not be subject to tax if you have ever made after-tax contributions to your IRA or plan.

For example, if some of your traditional IRA contributions were not tax-deductible, those contribution amounts will be income tax-free when you withdraw them from the IRA. This is simply because those dollars were already taxed once. You should consult a tax professional if your IRA or plan contains any after-tax contributions. (Special tax rules apply to Roth IRAs and Roth 401(k)/403(b) contributions.)

Caution: Taxable income from an IRA or retirement plan is taxed at ordinary income tax rates even if the funds represent long-term capital gains or qualifying dividends from stock held within the plan. There are special rules for capital gains treatment in some cases on distributions from retirement plans.

CAN RMDs IMPACT MY GIFT AND ESTATE TAX?

You first need to determine whether the federal gift and estate tax will apply to you. If you do not expect the value of your taxable estate to exceed the applicable exclusion amount, then federal gift and estate tax may not be a concern for you. However, state death (or inheritance) tax may be a concern. In some cases, your assets may be subject to more than one type of transfer tax – for example, the generation-skipping transfer tax may also apply. Consider getting professional advice to establish appropriate strategies to minimize your future gift and estate tax liability.

For example, you might reduce the value of your estate by gifting all or part of your required distribution to your spouse or others. Making gifts to your spouse can sometimes work well if your estate is larger than your spouse's, and one or both of you will leave an estate larger than the applicable exclusion amount. This strategy can provide your spouse with additional assets to better utilize their applicable exclusion amount, thereby minimizing the combined gift and estate tax liabilities of you and your spouse. Be sure to consult an estate planning attorney, however, about this and other possible strategies.

Caution: *In addition to federal gift and estate tax, your state may impose its own estate or death tax (or other transfer taxes). Consult an estate planning attorney for details.*

INHERITED IRAS AND RETIREMENT PLANS

Your RMDs from your IRA or plan will cease after your death, but your designated beneficiary (or beneficiaries) will then typically be required to take distributions from the account.

A spouse beneficiary may roll over an inherited IRA to their own account or treat it as their own IRA, allowing them to delay taking required minimum distributions until they turn age 72. They may also choose to leave it as a beneficiary IRA and begin taking distributions when the decedent spouse would have turned 72.

Most nonspousal beneficiaries are subject to the 10-year rule, which requires an IRA balance to be fully distributed by December 31 of the 10-year anniversary of the original owner's death. Note that employer plans such as 401(k)s may require a distribution sooner than 10 years.

There are a class of beneficiaries known as eligible designated beneficiaries that may still stretch distributions over their single life expectancy.

The distribution rules for inherited IRAs can be complicated, so seek your financial advisor or tax professional for additional guidance.

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