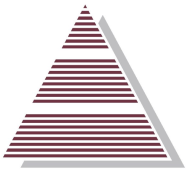

KARPUS
INVESTMENT
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COMMENTARY

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Required Minimum Distributions: What You Should Know and Possible Changes

During the last few decades, the employer-sponsored retirement savings landscape shifted away from defined benefit (pensions) to defined contribution plans (401k, 403b, etc.). This migration transitioned investment and lifetime income distribution responsibilities from the employer to the employee, forcing individuals to become more conscious of retirement savings rates, investment strategies, retirement income needs, and estate planning issues. In addition to employer-sponsored savings plans, individual retirement accounts (IRAs) were established as a tax-advantaged retirement savings account in 1974.

IRAs provide individual investors the opportunity to supplement employer retirement plans with personal, tax-advantaged investment accounts. Between 1995 and 2020, Americans' tax-advantaged accounts increased from $3 trillion to $22 trillion.

Since inception, IRAs have seen several changes to contribution limits and distribution requirements. Individuals previously concerned with saving as much as possible for retirement in tax-advantaged plans have a new-found concern: the pre and post-death taxable distribution of assets.

Most recently, the Setting Every Community Up for Retirement Enhancement Act (SECURE Act) was signed into law December 20, 2019 introducing several significant changes to IRA distribution rules. Subsequently, the IRS posted revised language in Publication 590-B in May 2021. Additional proposed regulations were announced in February 2022 further complicating how to interpret the new distribution rules. The Internal Revenue Service (IRS) is accepting comments and feedback on the proposed legislation until the end of May 2022 and final guidance is expected later this year.

At this time, we believe the important things to know about the SECURE Act and subsequent revisions and proposals are:

First, the SECURE Act created three distinct categories of beneficiaries:

1. Eligible Designated Beneficiaries
   - Minor Children of Decedent
   - Disabled Persons
   - Chronically Ill Persons
   - Not More Than 10 Years Younger than Decedent
   - Spouses
   - Certain Trusts
2. Non-Eligible Designated Beneficiaries
   - Non-Spouses
   - Certain Trusts
3. Non-Designated Beneficiary
   - Charities
   - Decedent's Estate (Naming Your Will)
   - Certain Trusts

The current understanding is as follows:

- Eligible beneficiaries will be allowed to use "Stretch" IRA provisions. This means that distributions will be based on their own life expectancy calculations using IRS Tables.
- Non-eligible beneficiaries are required to deplete inherited accounts by the end of the 10-year window following the account owner's death. There is significant uncertainty with this group depending on if the decedent died before or after taking required minimum distributions (RMDs).
- Non-designated beneficiaries are required to deplete inherited accounts by the end of the 5-year window following the account owner's death. There is significant uncertainty with this group depending on if the decedent died before or after taking RMDs.

The SECURE Act also made changes to these distribution rules:

- 10-Year Rule: eliminating the "Stretch IRA" option for non-eligible and non-designated beneficiaries. Further clarification is expected on this rule.
- Increasing the age retirement account owners must begin taking Required Minimum Distributions (RMDs) from accounts from 70 ½ to 72 for individuals born on or after July 1, 1949.
- Updated rules for distribution requirements for minors inheriting IRAs. Regardless of state rules, the 10-year distribution schedule will begin when the minor turns 21.

It is likely and expected that the IRS will provide additional guidance and clarification later this year. However, until that time the important takeaways remain: make sure you designate and/or update beneficiaries to match your planning objectives and current tax laws. The beneficiary designations that make sense today may not make sense in the future based on changes to your goals and objectives and changing tax laws. If possible, we advise reviewing your current beneficiaries at least annually.

To learn more about this topic or other Karpus insights, please take a look at our website for further information.

Sources: The Internal Revenue Service, Investopedia, Kitces, The Wall Street Journal

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