Required Minimum Distributions: A Tragedy in Three Acts

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The SECURE Act and CARES Act made significant changes to required minimum distributions (***RMDs***). What should you be doing to ensure your retirement plans are administered correctly? The first step is to understand your options. ***SECURE Act Shifts the Start*** Before the SECURE Act, RMDs had to begin by April 1st of the calendar year following the ***later of*** (i) the calendar year during which the participant retires or (ii) the calendar year in which the participant turns age 70; Following the passage of the SECURE Act, the age cutoff in that rule changed from age 70 to age 72, but only for individuals who turned age 70 on or after January 1, 2020 (*i.e.*, individuals born on or after July 1, 1949). In short, those terminated vested participants born ***before*** July 1, 1949 had to start their RMDs by April 1 of the year after turning 70, while those terminated vested participants born ***on or after*** July 1, 1949 could wait to begin RMDs until April 1st of the year after turning 72. By jumping from 70 to 72, this rule created a gap year in which the only trigger for someone to receive an initial RMD would be if he or she terminated employment after having turned age 70. **Example:** Joe, a vested terminated participant who was born at 11:55 p.m. on June 30, 1949, turns 70 in 2019. He has to begin his RMDs by April 1, 2020. Jenny, his vested terminated twin sister who was born ten minutes later at 12:05 a.m. on July 1, 1949, turns 72 in 2021. She has to begin her RMDs by April 1, 2022. So, who has to begin receiving RMDs on April 1, 2021? Only those individuals who (i) were born ***before*** July 1, 1949 and (ii) terminated employment in 2020. While the statutory cutoff age for RMDs will be 72 going forward, some employers (after consulting with their recordkeepers) have decided they prefer to maintain the status quo. The thought is that it is permissible to require distributions to commence after age 70, not because it's required under the Internal Revenue Code, but as a discretionary plan feature. But that's not the end of the story. For sponsors of defined contribution plans, the SECURE Act contained a bonus Easter egg provision: new rules limiting the timing of post-death RMDs to beneficiaries. Before the SECURE Act, a defined contribution plan could allow a designated beneficiary to stretch RMDs from a plan over the beneficiary's remaining life expectancy. The SECURE Act severely limited that option for participants who die after December 31, 2019. Under the SECURE Act changes, RMDs to designated beneficiaries are limited to payments over a ten-year period unless the designated beneficiary is not more than ten years younger than the participant, is disabled, chronically ill, or is the participant's surviving spouse or minor child. Designated beneficiaries in these categories may continue to receive RMDs over the beneficiary's expected lifetime except for minor children of the participant, for whom the ten-year rule begins to apply on the date that child reaches the age of majority. However, this change did not impact all plans. For those plans that require full distribution by December 31st of the fifth year following death (under the so-called alternative rule), no change in administration may be needed, though the standard RMD boilerplate language in the plan may need to be updated. ***CARES Act Complications*** Soon after the SECURE Act introduced this wrinkle into RMD administration, COVID-19 jumped to the forefront of public policy. Not wanting terminated employees to suffer the double whammy of losing their jobs and taking a distribution in a potentially virus-ravaged down market, the CARES Act included provisions which waived RMDs for 2020, including initial RMDs required to be taken in 2021 (for those seasoned employees terminating in 2020). But what did that ***really*** mean? Did it mean that distributions that would have been RMDs stayed in the plan? Maybe not. Employers had several options. They could make distributions as usual. They could not make distributions. They could make the distributions by default but give participants an option to opt out

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of distributions. Or they could not make distributions by default and give participants an option to opt in. The common denominator is that employers did not distribute RMDs If a plan continued to make distributions by default or a participant opted in, the participant received a distribution that only looked and smelled like an RMD. In fact, the distribution was ***not*** an RMD, but merely an eligible rollover distribution in RMD clothing. ***Next Steps for Employers*** The good news for employers in all this is that the deadline for adopting CARES Act and SECURE Act amendments is not until December 31, 2022 (for calendar year plans). So, if you haven't done so already, now is a great time to (i) examine how your plan was administered in 2020 with respect to the SECURE Act changes and CARES Act waivers, (ii) ensure that your SECURE Act and CARES Act plan amendments correspond to your past plan administration, and (iii) establish a prudent process for avoiding RMD failures in the future. Because there are so many ways plans could have been administered in 2020 and ***still be compliant*** with the RMD laws, if you act now, you should be able to keep your plan's document and administration in compliance. Plan sponsors are advised to consult the plan's counsel to determine what options are available.

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