JACOBI
CAPITAL MANAGEMENT

Required Minimum Distributions After Death: Non-Spouse Beneficiary

Funds in both traditional IRAs[1] and qualified retirement plans may not be kept inside these tax-deferred accounts indefinitely. Under federal law the money must eventually be distributed, and then taxed, through yearly "Required Minimum Distributions," or RMDs.[2]

The death of an account owner does not eliminate this requirement. However, the manner in which the assets must be distributed post-death will vary, depending primarily on:

- Death before or after required beginning date: During life, an account owner must generally begin distributions no later than April 1 of the year following the year he or she reaches age 70 ½. This is known as the "required beginning date," or RBD.[3]
- Who inherits the assets: The law mandates different required minimum distribution schedules depending on who inherits the assets in an account.

Non-Spouse Beneficiary Required Minimum Distributions

Owner Dies *Before* the Required Beginning Date

Situation	Distribution Requirement	Example
Individual beneficiary	RMDs for the beneficiary must begin by 12/31 of the year after year of death. Distributions are made over the beneficiary's life expectancy.	Paul dies in 2018 at age 67, leaving his IRA to his daughter Paulette, age 42. Paulette must begin to take RMDs by 12/31/19, using her age in 2019 of 43. The RMD for 2019 would be calculated by dividing the account balance on 12/31/18 by Paulette's age-43 life expectancy (from the Single Life Table) of 40.7.[4]

[1] For required minimum distribution purposes, the term "traditional IRA" also includes SIMPLE IRAs and SEP IRAs. Roth IRAs are subject to different rules.
[2] This discussion concerns federal income tax law. State or local law may vary.
[3] The RBD for qualified plan participants is April 1 of the year following the later of (a) the year the participant reaches age 70 ½, or (b) the year he or she retires. More than 5% owners must begin to receive distributions by April 1 of the year following the year they reach age 70 ½.
[4] The life expectancy factor is reduced by one for each year after the year of the first required distribution.

Situation	Distribution Requirement	Example
Multiple Beneficiaries (Assumes that the account is not divided into separate shares)	RMDs for the beneficiaries must begin by 12/31 of the year after the year of the owner's death. Distributions are made over the oldest beneficiary's life expectancy.	Paul dies in 2018 at age 67, leaving his IRA to his brother Bob, age 76, and his daughter Paulette, age 42. RMDs to them must begin by 12/31/19 and must be made over Bob's life expectancy as of his birthday in the year after Paul's death. The RMD for 2019 would be calculated by dividing the account balance on 12/31/18 by Bob's 2019 (Single Life Table) life expectancy, for age 77, of 12.1.[4]
No designated beneficiary, the owner's estate, a charity, or a non-qualifying trust	The entire amount must be distributed by the end of the fifth year after the owner dies.	Paul dies on 1/1/18, at age 68, leaving his IRA to his estate. The entire IRA balance must be distributed by 12/31/23.

Owner Dies *After* the Required Beginning Date

Situation	Distribution Requirement	Example
Individual beneficiary	RMDs for the beneficiary must begin by 12/31 of the year after year of death. Distributions are made over the longer of the owner's life expectancy, or the beneficiary's life expectancy.	Paul dies in 2018 at age 72, leaving his IRA to his older brother Bob, age 76. Because Paul has already passed his RBD, a distribution must be made for him for 2018. The RMD for 2018 is determined by dividing the account balance as of 12/31/17 by 25.6, the life expectancy (from the Uniform Lifetime Table) for a 72-year-old account owner. For 2019 and later years, the RMDs are calculated using the longer of the Single Life Table life expectancy for Paul in the year of his death, reduced by one (age 72 – 15.5-1=14.5) or Bob's life expectancy in the year after Paul's death (age 77=12.1). In this case, Paul's theoretical life expectancy is greater. The RMD for 2019 is calculated by dividing the account balance as of 12/31/18 by 14.5.[4]

Situation	Distribution Requirement	Example
Multiple Beneficiaries (Assumes that the account is not divided into separate shares)	An RMD must be made for the deceased owner for the year of death. RMDs for the beneficiaries must begin by 12/31 of the year after the year of death, with distributions over the longer of the owner's theoretical life expectancy or the oldest beneficiary's life expectancy.	Paul dies in 2018 at age 72, leaving his IRA to his son Peter, age 46, and his daughter Paulette, age 42. Because Paul has already passed his RBD, a distribution for 2018 must be made for him. This distribution is calculated by dividing the account balance as of 12.31.17 by 25.6, the life expectancy (from the Uniform Lifetime Table) for a 72 year old. For 2019 and later years, the RMDs are calculated using the longer of the Single Life Table life expectancy for Paul in the year of his death, reduced by one (age 72-15.5-1=14.5) or Peter's life expectancy (he's older than Paulette) in the year after Paul's death (age 47=37.0). In this case, Peter's life expectancy is the greater. The RMD for 2019 is calculated by dividing the account balance as of 12/31/18 by 37.0.[4]
No designated beneficiary, the owner's estate, a charity, or a non-qualifying trust	An RMD must be made for the deceased owner for the year of death. Thereafter, RMDs are based on the owner's theoretical life expectancy in the year of death.	Paul dies in 2018, at age 75, leaving his IRA entirely to charity. An RMD must be made for him for 2018, calculated using his age 75 life expectancy (from the Uniform Lifetime Table) of 22.9. For 2019 and later years, Paul's life expectancy in the year of his death (from the Single Life Table), reduced by one for each subsequent year, is used to calculate the RMD. For 2019, Paul's life expectancy would be 12.4 (his 2018 life expectancy at age 75 of 13.4-1).[4]

Other Distribution Options

Funds in an inherited IRA or qualified retirement plan may also be distributed as a single lump-sum or as periodic or occasional distributions which withdraw the money at a rate faster than the RMDs required by federal tax law. However, such accelerated distributions will subject the funds to current income tax more quickly than will the RMD withdrawals.

Post-Mortem Distribution Planning

IRAs and qualified plans allow an account owner to name a beneficiary or beneficiaries to receive the account proceeds should the owner die. From this pool of potential inheritors, IRS regulations require that the individual or group of individuals who will ultimately receive the funds, the "designated beneficiaries," be identified by September 30 of the year following the year of death.

This time delay allows for a certain amount of post-death estate and income tax planning by "removing" a potential beneficiary through either a qualified disclaimer, a cash distribution, or by dividing the IRA or qualified plan into separate accounts. Any separate accounts must generally be established by December 31 of the year following the year of the account owner's death. The life expectancies of those beneficiaries who remain on September 30 are then used to determine the RMDs for the years after death.

Entities without a measurable life span, such as the owner's estate, a charity, or a trust that does not meet certain IRS requirements, are not considered to be "designated beneficiaries" for RMD purposes. While such beneficiaries may inherit the funds in the account, distributions to these entities are generally made on less favorable terms.

Trusts

In order for the beneficiaries of a trust to qualify as a "designated beneficiaries," the trust must meet certain requirements:

- The trust must be valid under state law;
- The trust must be irrevocable or will, under its terms, become irrevocable upon the death of the account owner;
- The beneficiaries of the trust must be identifiable from the trust document; and
- Certain documents must be provided to the plan administrator.[5]

Distributions to the trust are made over the theoretical life expectancy of the beneficiary. If there is more than one beneficiary, distributions are made over the theoretical life expectancy of the oldest beneficiary.

If a trust does not meet these requirements, consideration should be given to reforming the trust, assigning or disclaiming an interest in the trust, cashing-out certain beneficiaries, or separating interests in the trust.

Other Points

- Distributions from employer-sponsored qualified plans: Post-death payments to beneficiaries of qualified plans are typically based on the individual provisions of a particular plan. A lump-sum distribution, with its heavy, immediate taxation, is perhaps the most frequently encountered option.

  The Pension Protection Act of 2006, effective for distributions after December 31, 2006, provides for a direct trustee-to-trustee transfer from a qualified plan to an IRA specifically designed to receive retirement assets inherited by a non-spouse beneficiary. The non-spouse beneficiary is not treated as the owner of the rolled-over assets and the assets may not be rolled-over to another account. Required minimum distributions are made from the "inherited IRA" in accordance with the normal rules applicable to non-spouse beneficiaries.

  Such an after-death transfer has the same result as if the decedent had moved the assets in his or her qualified plan into an IRA rollover prior to death.

[5] Generally, this must occur by October 31 of the year following the year of death.

Roth IRAs

Roth IRAs do not have a lifetime distribution requirements. Because of this, a Roth IRA owner is always viewed as having died before the RBD. Post-death distributions from Roth IRAs are thus governed by the "death before RBD" rules.

Seek Professional Guidance

The body of law and regulation surrounding required minimum distributions is complex and often confusing. Further, the failure to correctly distribute the required amounts from an IRA or qualified plan can result in a federal excise tax of 50% of the amount that should have been distributed. Individual state or local law may also provide penalties.

The advice and guidance of qualified professionals is strongly recommended.