CARLTON FIELDS

IRS Clarifies Application of Required Minimum Distribution Rules to Inherited Retirement Accounts

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The Secure Act, passed in 2019 and updated in 2022, made significant changes to the required minimum distribution (RMD) rules applicable to qualified retirement plans, IRAs, 403(b) plans, and other eligible deferred compensation plans. In addition to increasing the age for RMD-required beginning dates, the Secure Act required the full distribution of the account balances from these plans within 10 years of an account holder's death for most non-spouse designated beneficiaries, regardless of whether distributions had begun. Prior to the final regulation, there was confusion as to whether a designated beneficiary of an inherited account had to take RMDs during the 10-year period or whether he or she could wait to receive the entire account balance at the end of the 10-year period. The final regulations, which became effective on September 17, 2024, provide clarity. Designated beneficiaries are individuals designated by an account holder as beneficiaries other than those who are considered "eligible designated beneficiaries." Eligible designated beneficiaries include a surviving spouse, a minor child of the deceased account holder, a chronically ill individual as defined by Internal Revenue Code section 72(m), a disabled person as defined by section 7702B(c)(2) of the Internal Revenue Code, or a person not more than 10 years younger than the deceased account holder. Spouses and other eligible designated beneficiaries have more options than designated beneficiaries regarding distributions from an inherited account. Spouse beneficiaries have the most options. If an account holder dies before the RMD-required beginning date, the spouse beneficiary may: (1) keep the account as an inherited account; (2) delay starting distributions until the account holder would have reached the RMD-required beginning date; (3) take distributions based on his or her own life expectancy; (4) follow the 10-year rule; or (5) roll the funds into an IRA in his or her own name. If the account holder's death occurs after the RMD-required beginning date, the spouse beneficiary may: (1) keep the account as an inherited account; or (2) take distributions based on his or her own life expectancy or roll over the account into an IRA in his or her own name. Non-spouse-eligible designated beneficiaries may take distributions over the longer of their own life expectancy or the account holder's remaining life expectancy. Alternatively, the eligible designated beneficiary may follow the 10-year rule if the account holder dies before his or her RMD-required beginning date. For all other designated beneficiaries, although they must follow the 10-year rule, there was confusion as to whether they were required to take RMDs during the 10 years or could wait until the end of the 10-year period before taking the entire distribution. The final regulations clarify this confusion by providing: (1) if an account holder dies on or after his or her RMD-required beginning date, RMDs must be taken each year for the 10 years until the total distribution is received; and (2) if an account holder dies before the RMD-required beginning date (or if the entire account is in a designated Roth account), the designated beneficiary does not have to take RMDs annually and can wait until the 10th year to take the entire distribution. Because of the confusion about RMDs and the 10-year rule, the IRS granted relief under Notice 2022-53 for beneficiaries subject to the 10-year rule who failed to take an RMD from an inherited account for both 2021 and 2022. Please reach out if you have questions about the implementation of the new RMD rules. We are here to help.

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