MEMO# 35798

July 31, 2024

Treasury and IRS Finalize Amendments to Regulations Governing Required Minimum Distributions from Retirement Plans and Issue Related Proposed Regulations

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TO: ICI Members
Pension Committee
Pension Operations Advisory Committee SUBJECTS: Pension
Tax RE: Treasury and IRS Finalize Amendments to Regulations Governing Required Minimum Distributions from Retirement Plans and Issue Related Proposed Regulations

The IRS and Treasury have released a long-awaited set of rulemakings to amend the regulations governing required minimum distributions (RMDs) from retirement plans and IRAs. The first piece is a final regulation that reflects changes made by the Setting Every Community Up for Retirement Enhancement Act (the SECURE Act) of 2019 and other legislation over the years.[1] The final rule leaves several provisions reserved to be addressed by a proposed regulation,[2] which is the second piece of the set, which addresses changes made by the SECURE 2.0 Act.

Comments on the new proposed regulations are due September 17, 2024. IRS also announced that they have scheduled a public hearing on the proposed regulation for September 25, 2024.

Background

Section 401(a)(9) of the Internal Revenue Code (Code) provides rules for required distributions from tax-qualified retirement plans, both during the life of the employee and after the death of the employee. The rules prescribe a required beginning date for distributions and identify the period over which the interest in the retirement plan must be distributed. The RMD rules for qualified plans are adopted by reference in Code sections 408 (for IRAs), 408A (for Roth IRAs), 403(b) (for 403(b) plans), and 457(d) (for eligible deferred compensation plans).

The SECURE Act made a number of changes to the RMD rules for IRAs, qualified plans, 403(b) plans, and 457(b) plans, as set forth in section 401(a)(9) of the Code.[3]

- Increase Age for Required Minimum Distributions. Section 114 of the SECURE Act increased the age at which RMDs must begin, from age 70½ to age 72. The provision became effective for distributions required to be made after December 31, 2019, with respect to individuals who attain age 70½ after December 31, 2019.
- Modify RMD Rules for Beneficiary Payments. Section 401 of the SECURE Act modified the RMD rules for post-death distributions from defined contribution (DC) plans and IRAs to beneficiaries. It generally requires the account to be fully distributed within 10 years following the year of the participant's or IRA owner's death, unless the distribution is made to an "eligible designated beneficiary" (i.e., a surviving spouse, a disabled or chronically ill individual, an individual who is not more than ten years younger than the participant or IRA owner, or a child of the participant or IRA owner who has not reached the age of majority). Eligible designated beneficiaries can continue to "stretch" RMD payments over life expectancy. This section is generally effective for RMDs with respect to employees (or IRA owners) with a date of death after December 31, 2019, although there are special rules for certain situations and a delayed effective date for governmental and collectively bargained plans.

IRS published proposed regulations on February 24, 2022, both to implement the SECURE Act changes and to address other statutory changes to the rollover rules of Code section 402(c) that have been made since regulations were first issued.[4] ICI submitted a comment letter on May 25, 2022 suggesting several changes to the 2022 proposal.[5]

In advance of issuing the final regulations, IRS provided relief regarding missed RMDs related to the proposal's unexpected interpretation (discussed below) of changes made by the SECURE Act to the RMD rules for post-death distributions from DC plans and IRAs to beneficiaries (requiring annual distributions alongside the 10-year rule for certain beneficiaries).[6]

After the close of the comment period on the 2022 proposed rules, Congress enacted the SECURE 2.0 Act (in December 2022), which made further changes to the RMD rules, affecting many of the provisions included in the proposed regulations.[7]

- Increase in age for required beginning date for mandatory distributions. For individuals who attain age 72 after December 31, 2022 and attain age 73 before January 1, 2033, Section 107 of the SECURE 2.0 Act increases the required minimum distribution (RMD) age to 73, effective for distributions required to be made after December 31, 2022. The Act increases the age further to 75 starting on January 1, 2033
- Qualifying longevity annuity contracts. Effective for contracts purchased or received in an exchange on the date of enactment, Section 202 of the SECURE 2.0 Act modifies the rules for qualifying longevity annuity contracts (QLACs) to remove the existing 25 percent limit on the amount of QLAC premiums that can be excluded from RMD rules and raise the existing $145,000 limit on such premiums to $200,000 (indexed).[8]
- Eliminating a penalty on partial annuitization. Section 204 of the SECURE 2.0 Act directs Treasury to amend the regulations governing RMDs to provide that when an individual account plan participant uses a portion of their account to purchase an annuity, the plan may allow the employee to elect to have the RMD amount for a year calculated as the excess of (i) the total required amount for such year (i.e., treating the account balance as of the last valuation date in the immediately preceding

calendar year as including the value on that date of all annuity contracts which were purchased with a portion of the account) over (ii) the total amount distributed in the year from all such annuity contracts.
- Reduction in excise tax on certain accumulations in qualified retirement plans. Effective for taxable years beginning after the date of enactment, Section 302 of the SECURE 2.0 Act reduces the penalty for failure to take an RMD from a plan or IRA from 50 percent to 25 percent and further reduces the penalty to 10 percent where the taxpayer corrects the failure during a specified correction window by receiving a distribution from the same plan or IRA to which the tax relates.
- Roth plan distribution rules. Section 325 of the SECURE 2.0 Act harmonizes the RMD rules for Roth amounts in plans and IRAs by exempting Roth amounts in plans from RMD requirements during the life of the participant, effective for taxable years beginning after December 31, 2023.[9]
- Surviving spouse election to be treated as employee. Section 327 of the SECURE 2.0 Act harmonizes the RMD rules applicable to surviving spouses under plans and IRAs by allowing a surviving spouse beneficiary under a plan to elect to be treated as the deceased employee for purposes of the RMD rules, effective for calendar years beginning after 2023. As a result, the spouse is able to receive a similar distribution period for lifetime distributions under an employer-sponsored retirement plan as is currently permitted in an IRA.

Final Rule

While certain changes were made in response to comments received and to incorporate provisions from the SECURE 2.0 Act, the final regulations generally follow the proposed regulations issued in 2022.

Like the 2022 proposal, in addition to updating the existing regulations under Code sections 401(a)(9), 402(c), 403(b), 457, and 4974 to reflect statutory amendments that have been made since those regulations were last issued, the final rule also clarifies certain issues that had been raised in public comments and private letter ruling requests. The final rule retains the 2022 proposal's replacement of the question-and-answer format of the existing regulations under Code sections 401(a)(9), 402(c), 408, and 4974 with a standard format similar to more recent IRS/Treasury regulations.

Section 401(a)(9) Regulation Amendments (RMDs)

The final regulations address the following issues, among others, under the Code section 401(a)(9) rules.

Issues related to distributions to the employee/IRA owner:

- RMDs commencing during the lifetime of the employee. The proposal confirmed that the updated required beginning date (generally April 1 of the calendar year following the later of the calendar year in which the employee attains age 72 or the calendar year in which the employee retires) applies to employees born on or after July 1, 1949. The final rule incorporates the additional changes to the required beginning date made by section 107 of the SECURE 2.0 Act. The final rule removes the proposal's reference to "age 72" and replaces it with the term "applicable age." A new definition of applicable age indicates which age will apply (age 70 ½, 72, 73 or 75), according to the employee's date of birth. The final rule reserves a section for employees born in 1959 (see proposed rule, below). The final rule also adds clarifying language that, where a participant in a multiple employer plan retires from one employer participating in the plan but is employed by a different employer participating in the same plan, that employee will not be treated as having retired (i.e., the employee will not yet need to begin taking RMDs from the plan).[10]

- Ability for plan to use universal beginning date. In the preamble, in response to a question from a commenter, the IRS notes that while a plan cannot simply provide a uniform required beginning date of April 1 of the calendar year following the year an employee attains age 70 ½ and apply this required beginning date to all employees in the plan, a plan could require benefits to commence by that date.[11] This seems to be an acknowledgment that as a matter of plan design, plans are permitted to require distributions as early as the plan's normal retirement age, or age 62, if later. Therefore, a plan could set a requirement that distributions must begin by age 71 ½, however, any distributions before the individual's applicable required beginning date would not be treated as RMDs.[12]
- RMDs for designated Roth accounts. The final regulations incorporate section 325 of the SECURE 2.0 Act (for a designated Roth account, no RMDs are required during the employee's lifetime), providing that for calendar years up to and including the year of the employee's death, amounts held in a designated Roth account are not taken into account for calculating the RMD. Where the employee's entire interest in the DC plan is in a designated Roth account, upon the employee's death, the employee is treated as having died before his or her required beginning date. As discussed below, the proposed rule addresses how distributions (during the employee's lifetime) from designated Roth accounts are treated.

Issues related to distributions to beneficiaries:

- Application of the January 1, 2020 effective date for the limitation on life expectancy distributions to beneficiaries. Like the 2022 proposal, the final regulations include various scenarios illustrating the impact of the timing of the employee's or designated beneficiary's death on the application of the statutory effective date for section 401 of the SECURE Act.
- Application of the new 10-year rule when the employee dies before the required beginning date. The proposal clarified that, under the 10-year rule, the employee's entire interest in a DC plan must be distributed by the end of the calendar year that includes the tenth anniversary of the employee's death (as opposed to 10 years from the date of death). The proposal also provided that for eligible designated beneficiaries of an employee who dies prior to the required beginning date, the plan may provide either that the 10-year rule applies or that the life expectancy payments rule applies. Alternatively, in this situation, the plan may provide the employee or the eligible designated beneficiary an election between the 10-year rule or the life expectancy payments rule. However, if a DC plan does not include either of those optional provisions and the employee has an eligible designated beneficiary, the plan must provide for the life expectancy payments rule. The final regulation retains these provisions and clarifies that a DC plan may provide that a particular distribution method will apply to certain categories of eligible designated beneficiaries or that an election method is only available for certain categories of eligible designated beneficiaries.[13]
- Determination of designated beneficiaries, including eligible designated beneficiaries. For purposes of identifying an eligible designated beneficiary who is a minor child of the employee, the proposal defined "age of majority" as the child's 21st birthday.[14] The final regulations add a reference to the Code section 152(f)(1) definition of "child," confirming that "minor child" for this purpose includes stepchildren, adopted children,

and foster children. The proposal also included a definition of "disability" and provided that the determination of whether a beneficiary is disabled is made as of the date of the employee's death. With respect to a beneficiary who is disabled or chronically ill as of the date of the employee's death, the proposal required documentation of the disability or chronic illness to be provided to the plan administrator no later than October 31 of the calendar year following the calendar year of the employee's death. Our comment letter urged Treasury and IRS to allow plans and IRA providers to rely on a beneficiary's representation that he or she satisfies the definition of disabled or chronically ill. The final regulations retain the requirement to provide documentation to a plan administrator;[15] however, in the case of an IRA, there is no longer a requirement to provide documentation of disability or chronic illness to the IRA custodian, issuer, or trustee.

- Special considerations for trust beneficiaries. The proposal contained detailed rules relating to trusts as beneficiaries, including rules for "see-through trusts" (such as determining which beneficiaries of see-through trusts will be treated as the employee's beneficiary and meeting the identifiability requirements for see-through trusts). The proposal also fleshed out the requirements for "applicable multi-beneficiary trusts" (as created by the SECURE Act section 401) benefitting disabled or chronically-ill individuals. The final regulations adopt these provisions with some modifications in response to comments.
- Other rules for designated beneficiaries and eligible designated beneficiaries. If an employee has more than one designated beneficiary and at least one of them is not an eligible designated beneficiary, the proposal indicated that the employee generally is treated as not having an eligible designated beneficiary. The proposal provided special exceptions to this general rule, however, when either (1) one of the designated beneficiaries is a minor child of the employee or (2) the beneficiary is an applicable multi-beneficiary trust benefitting disabled or chronically-ill individuals and meeting certain requirements. For purposes of identifying designated beneficiaries, the proposal provided an exclusive list of events that (if occurring within a specified time period) permit disregard of a beneficiary who was a beneficiary as of the employee's date of death (such as the beneficiary making a qualified disclaimer). The final rule retained these provisions.
- Eligible designated beneficiaries who are older than the account owner. Under the proposal, for an eligible designated beneficiary who is older than the IRA owner/employee (and where the owner/employee dies after the required beginning date), the eligible designated beneficiary may use the owner's/employee's remaining life expectancy to calculate annual distributions. However, the proposal provided that the entire remaining amount must be distributed by the end of the calendar year in which the beneficiary's remaining life expectancy is less than or equal to one. Our comment letter urged Treasury and IRS to eliminate this special rule requiring accelerated distribution. Treasury and IRS agreed to this change.[16]
- Special rules applicable to RMDs from DC plans. The proposal included guidance for calculating RMDs under the life expectancy rule. In addition, this section included a controversial interpretation of the SECURE Act that would require annual distributions in certain circumstances when the new 10-year rule applies (under the 10-year rule, the employee's entire interest in a DC plan must be distributed by the end of the calendar year that includes the tenth anniversary of the employee's death). Specifically, the proposal provided that when an employee dies after the required beginning date with a designated beneficiary who is not an "eligible designated beneficiary," then the designated beneficiary would continue to have annual RMDs calculated using the beneficiary's life expectancy as under the existing regulations for

up to nine calendar years after the employee's death. In the tenth year following the calendar year of the employee's death, a full distribution of the employee's remaining interest would be required. The same annual payout rule would apply to the designated beneficiary of an eligible designated beneficiary who dies before the entire interest is distributed. Despite strong pushback from commenters (including ICI's comment letter), the IRS declined to change its interpretation in the final rule. As mentioned above, IRS has provided transition relief through 2024, under which plans and IRAs will not be treated as violating the RMD rules because of missed annual distributions due to this interpretation.[17]

For employees with multiple designated beneficiaries, like the proposal, the final rule generally requires use of the life expectancy of the oldest designated beneficiary (rather than the beneficiary with the shortest life expectancy, as provided in the existing regulation) for determining the applicable denominator, subject to certain exceptions. Similarly, for situations where the employee has more than one beneficiary and life expectancy distributions apply (e.g., all of the employee's beneficiaries are eligible designated beneficiaries), the 10-year rule would be triggered upon the death of the oldest designated beneficiary. Our comment letter recommended that Treasury and IRS reconsider the "death of oldest beneficiary" trigger for application of the 10-year rule in these situations; however, the final regulation retains this rule.[18]

The final regulations also include changes to implement sections 202 (modifying the limits for QLACs) and 204 (calculation of RMD amount for partial annuitization of individual account)[19] of the SECURE 2.0 Act.

Section 402(c) Regulation Amendments (Rollovers)

The proposal amended the Code section 402(c) regulation to reflect various statutory changes made since 1995, such as changes made by the Economic Growth and Tax Relief Reconciliation Act of 2001 and the Pension Protection Act of 2006.[20] The proposed amendments also included changes to reflect the new SECURE Act RMD rules for distributions to beneficiaries, which are relevant in determining amounts eligible for rollover. For example, the proposal provided that when the 10-year rule applies with respect to an employee who dies before the required beginning date, no amount distributed before the tenth calendar year after the calendar year of the employee's death is treated as an RMD. In that situation, in the tenth calendar year after the calendar year of the employee's death, the entire amount distributed in that year is treated as an RMD (and thus is not an eligible rollover distribution). In situations where the employee dies on or after the required beginning date and annual distributions are required (either ongoing or in years one through nine), the proposal provided that the amount of the RMD is calculated pursuant to the rules described earlier and would not be an eligible rollover distribution.

Among the changes to the proposal,[21] the final regulations provide that when a distribution is made directly to a non-spouse beneficiary rather than transferred directly to an inherited IRA, then the distribution is still subject to 20 percent withholding as an eligible rollover distribution, even though the direct distribution cannot then be rolled over.[22]

Section 403(b) Regulation Amendments

Because 403(b) plans must satisfy RMD rules similar to the requirements of Code section 401(a)(9), the proposal makes conforming changes to the 403(b) regulations to reflect the SECURE Act changes. The proposal notes that specific RMD requirements applicable to

403(b) plans in some instances track the RMD rules for IRAs, and in other instances track the rules for qualified plans (such as 401(k) plans). For example, like in the IRA context, an RMD owed from one 403(b) plan account may be satisfied through a distribution from another 403(b) account of the taxpayer. However, the required beginning date applicable to a 403(b) plan account is determined in the same manner as a qualified plan required beginning date. The final regulations are the same as the proposed, except for a few minor changes.[23]

In the preamble to the proposed regulations, the Treasury Department and IRS indicated that they were considering additional changes so that the RMD rules for 403(b) plans would more closely follow the RMD rules for qualified plans. Our comment letter strongly recommended against conforming the RMD rules for 403(b) plans to the RMD rules applicable to tax-qualified plans, noting that there are structural and administrative differences between the two types of plans that would make importation of the tax-qualified plan rules unworkable. The final regulation does not include any such conforming changes. However, in the preamble to the final regulations, the Treasury Department and IRS explain that they "are considering [the comments received in response to the comment request], and any further changes relating to the required minimum distribution rules for section 403(b) plans will be set forth in separate guidance."[24]

Section 408 Regulation Amendments (IRAs)

The proposal amended the IRA regulations under Code section 408 to reflect the SECURE Act changes (such as the updated required beginning date) and other prior guidance. As part of these updates, when a beneficiary transfers amounts from a plan to an inherited IRA in the name of the decedent, the proposed regulation provided for comparable treatment between non-spouse beneficiaries and spousal beneficiaries in terms of carry-over of the elected distribution method. For example, if an employee dies before the required beginning date after designating the employee's spouse as a beneficiary, and the surviving spouse rolls over a distribution from the qualified plan to an IRA in the name of the decedent, then any distribution method that was elected under the qualified plan also will apply to the IRA that receives the rollover. The same rule applies under the proposal where the distributing plan is an IRA. The proposal also described comparable rules for spouse and non-spouse beneficiaries in applying the deadline for making an election between the 10-year rule and life expectancy rule. The proposal, however, allowed a surviving spouse making a transfer to an inherited IRA to elect to use the life expectancy rule even if the distributing plan would have required distributions under the 10-year rule (or 5-year rule as applicable). The final rule retains these provisions.

With respect to the ability of a surviving spouse to instead elect to treat a decedent's IRA as the spouse's own IRA, the proposal provided that the deadline for making such an election is the later of (1) the end of the calendar year in which the surviving spouse reaches age 72, and (2) the end of the calendar year following the calendar year of the IRA owner's death. If the spouse did not make such an election by the deadline, he or she still may elect to roll over distributions to his or her own IRA at a later time but (under the proposal) would have been subject to a special recapture rule for distributions that hypothetically would have been required after the spouse's required beginning date. The spouse would not be able to roll over these hypothetical RMDs to the IRA.

Our comment letter argued that the requirement to calculate hypothetical RMDs if a spouse later rolls over to his or her own IRA, adds unnecessary complexity to already complex rules and we urged Treasury to eliminate this requirement. In the final regulation, Treasury eliminates the deadline for electing to treat a decedent's IRA as the spouse's own IRA and instead provides a new timing rule. The timing rule applies on a yearly basis and essentially provides that the surviving spouse can only make the election to treat the IRA as their own in any calendar year after the amounts treated as RMDs under section 1.402(c)-2(j)(4)(ii)[25] for that year have been distributed from the IRA. As described below, the new proposed rule includes an example to illustrate the application of this rule.

The final regulations clarify how the aggregation rules[26] apply when an owner of multiple IRAs dies before taking the sum of the RMDs that are required for the year and where the IRAs do not all have identical beneficiary designations. In this situation, each IRA must distribute a proportional share of the shortfall of the total RMD amount that remains unpaid for the year.

Section 457(b) Regulation Amendments

In response to questions from commenters, the final regulations clarify that, if an eligible deferred compensation plan is subject to the rules of § 1.401(a)(9)-5, then the plan must also satisfy the rules of section 401(a)(9)(H) (i.e., the new 10-year rule), without regard to whether the plan is maintained by a tax-exempt entity.

Section 4974 Regulation Amendments (Excise Tax)

The 2022 proposal updated the excise tax provisions for the SECURE Act changes, including the 10-year rule. In addition, the proposal provided for two situations in which an automatic waiver of the excise tax will apply (one of which is based on the existing regulation). The two situations involve: (1) an employee or IRA owner who dies prior to the required beginning date with an eligible designated beneficiary who is subject to the life expectancy rule (pursuant to the plan document or regulatory default) but who elects instead to use the 10-year rule; and (2) an individual who had an RMD due in a calendar year but who dies in that calendar year prior to taking the distribution, with a beneficiary who also does not take the RMD in that calendar year as required (but who does take the distribution by the beneficiary's tax filing deadline, including extensions). An automatic waiver will apply in these situations if the applicable conditions are met.

The final regulation retains these changes, with one modification in response to comments. For situation (2) above in which an automatic waiver will apply, the deadline for the beneficiary to take the missed RMD is extended under the final rule to the later of the tax filing deadline for the taxable year of the beneficiary that begins with or within the calendar year in which the individual died and the end of the following calendar year.

The final regulations also reflect changes made by section 302 of the SECURE 2.0 Act. Section 302(a) reduces the penalty for failure to take an RMD from a plan or IRA from 50 percent to 25 percent. Section 302(b) further reduces the penalty to 10 percent where the taxpayer corrects the failure during a specified correction window[27] by receiving a distribution from the same plan or IRA to which the tax relates.[28] As discussed below, the proposed rule addresses how these corrective distributions should be treated.

Proposed Rule

The final rule left several provisions reserved to be addressed by the proposed regulation. The proposed regulations address SECURE 2.0 Act sections 107 (increase in RMD age to 73 in 2023 and 75 in 2033), 202 (changes to QLAC rules), 204 (calculation of RMD amount for partial annuitization of individual account), 302 (reduction of penalty for RMD failures), 325 (exempting Roth amounts in plans from RMD requirements during the life of the participant), and 327 (allowing a surviving spouse beneficiary under a plan to elect to be treated as the deceased employee for purposes of the RMD rules).

More specifically, the proposal addresses the following:

Determination of Applicable Age for Employees Born in 1959

Section 107 of the SECURE 2.0 Act, which raises the age for beginning RMDs in two steps, contains a drafting error impacting individuals born in 1959, who will turn 73 in 2032. In this case, it is unclear whether the individual's RMD age is 73 or 75. Members of Congress have indicated that the RMD age for such individual is 73.[29] In other words, Congress intended to increase the applicable age from 73 to 75 for individuals who turn 73 after December 31, 2032. Under the proposed regulations, the applicable age for an employee who was born in 1959 would be 73.

Purchase of Annuity Contract with Portion of Employee's Individual Account - Rules of Operation for Aggregation Option

To implement section 204 of the SECURE 2.0 Act, the final rule addresses how to calculate RMDs where an individual annuitizes a portion of their account balance. Instead of satisfying the RMD rules separately for the annuity contract purchased with a portion of the account and the remaining account balance, the final rule permits the employee to aggregate the two portions by adding the fair market value of the annuity contract to the remaining account balance and treating payments under the annuity contract as distributions from the account. The final rule reserves discussion of how this aggregation operates.

The proposed regulations set forth rules for the operation of this aggregation option. The fair market value of the annuity contract would be determined as of December 31 of the prior calendar year for purposes of each distribution, with fair market value (for distributions taking place as of 2026) determined pursuant to the rules for determining the fair market value of a traditional IRA that is an individual retirement annuity if that IRA is converted to a Roth IRA.[30]

Distributions from Designated Roth Accounts

The final rule incorporates section 325 of the SECURE 2.0 Act (providing that for a designated Roth account, no RMDs are required during the employee's lifetime), but does not address the treatment of pre-death distributions from designated Roth accounts for purposes of satisfying the RMD rules with respect to non-Roth accounts under the plan.

The proposed regulations provide that a distribution from a designated Roth account, made in a calendar year during which an employee must take a RMD under the plan, will not count towards the RMD requirement. Preamble language confirms that because such distributions are not treated as RMDs, they may be rolled over to a Roth IRA.

Corrective Distributions Giving Rise to Reduction or Waiver of the Section 4974 Excise Tax

To implement section 302(b) of the SECURE 2.0 Act, the final rule addresses the excise tax reductions (for failure to take an RMD) as discussed above, reserving the treatment of corrective distributions that give rise to a reduction or waiver of the section 4974 excise tax.[31]

Under the proposed regulations, a corrective distribution would not be taken into account when determining whether the RMD rules are met for the calendar year in which the corrective distribution is made. The corrective distribution is nonetheless treated as a RMD (for the prior year in which the RMD was missed) —and as such is not eligible for rollover.

Spousal Election Under Section 327 of the SECURE 2.0 Act

The final rule implements section 327 of the SECURE 2.0 Act by allowing a surviving spouse to elect to be treated as the deceased employee for purposes of the required minimum distribution rules.

The proposed regulations provide a number of clarifying rules relating to this election, including addressing when the election applies automatically and when plans may use a default election. The proposed regulation also provides:

- that the spousal election is available only if the first year for which annual RMDs to the surviving spouse must be made is 2024 or later;
- that the spouse is not treated as the employee for all purposes (e.g., the spouse may take a distribution before reaching age 59 ½); and
- that amounts in a designated Roth account will be included in the RMD calculation.

The proposed regulation also includes an example of the hypothetical RMD calculation for determining the amount that must be distributed before the spouse may roll over the account balance to their own IRA.

Divorce After Purchase of Qualifying Longevity Annuity Contract (QLAC)

Section 202 of the SECURE 2.0 Act provides that in the case of a joint and survivor QLAC, if a divorce occurs after the QLAC purchase and before payments have commenced, the divorce will not affect the permissibility of the joint and survivor benefits if conditions related to a qualified domestic relations order (QDRO) are met. The final rule reserves for consideration rules relating to a divorce or separation instrument that may be substituted for a QDRO in the case of arrangements that are not subject to the QDRO requirements of ERISA and the Code (such as governmental plans).

The proposed regulations clarify what documents qualify as a "divorce or separation instrument."

Outright Distribution to Trust Beneficiary

The final rule addresses the application of Code section 401(a)(9) to multiple beneficiaries of a see-through trust. The proposed regulations expand on the final rule, detailing an exception to the requirement that the trust provide it will be divided immediately upon the death of the employee, with separate interests to be held in separate see-through trusts.

Applicability Dates

The 2022 proposal was proposed to apply beginning January 1, 2022. Our comment letter urged IRS to delay the applicability date of the amended regulations, noting that many of the interpretations introduced by the proposal were unexpected and would take time to incorporate into practice.[32]

The final rule will be effective September 17, 2024. The final regulations under IRC section 401(a)(9) apply for distribution calendar years beginning on or after January 1, 2025. For earlier distribution calendar years, taxpayers must apply the 2002 final regulations and 2004 final regulations, but taking into account a reasonable, good faith interpretation of the amendments made by SECURE Act sections 114 (increased RMD age) and 401 (modification of rules for post-death distributions to beneficiaries) (compliance with the 2022 proposed regulations will suffice). For the 2023 and 2024 distribution calendar years, taxpayers must also take into account a reasonable, good faith interpretation of the amendments made by SECURE 2.0 Act sections 107 (increase in RMD age to 73), 201 (modification of RMD rules for annuities), 202 (changes to QLAC rules), 204 (calculation of RMD amount for partial annuitization of individual account), and 337 (modification of RMD rules for special needs trust). The amendments to the rollover rules under IRC section 402(c) are applicable for distributions on or after January 1, 2025, and the amendments relating to the RMD excise tax provisions under IRC section 4974 are applicable for taxable years beginning on or after January 1, 2025.

The proposed rules are proposed to have the same applicability dates as the corresponding provisions in the 2024 final regulations (e.g., distributions for years beginning on or after January 1, 2025).

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Notes

[1] The final rule was published at 89 Fed. Reg. 58886 (July 19, 2024), available at https://www.govinfo.gov/content/pkg/FR-2024-07-19/pdf/2024-14542.pdf.

[2] The proposed rule was published at 89 Fed. Reg. 58644 (July 19, 2024), available at https://www.govinfo.gov/content/pkg/FR-2024-07-19/pdf/2024-14543.pdf.

[3] For a summary of the SECURE Act, see ICI Memorandum No. 32118, dated December 20, 2019, available at https://www.ici.org/memo32118.

[4] For background and a description of the 2022 proposal, see ICI Memorandum No. 34057, dated March 4, 2022, available at https://www.ici.org/memo34057-0.

[5] For an overview of the comment letter, see ICI Memorandum No. 34160, dated May 25, 2022, available at https://www.ici.org/memo34160.

[6] For an overview of Notice 2022-53, which included the initial transition relief, see ICI Memorandum No. 34307, dated October 10, 2022, available at https://www.ici.org/memo34307. The IRS subsequently extended this relief through 2024 in Notices 2023-54 and 2024-35. For a summary of Notice 2023-54, see ICI Memorandum No. 35378, dated July 19, 2023, available at https://www.ici.org/memo35378. For a summary of Notice 2024-35, see ICI Memorandum No, 35682, dated April 16, 2024, available at https://www.ici.org/memo35682.

[7] For a summary of the SECURE 2.0 Act, see ICI Memorandum No. 34795, dated January

12, 2023, available at https://www.ici.org/memo34795.

[8] The Act directs Treasury to amend the QLAC regulations to reflect these changes no later than 18 months after the date of enactment and permits reliance on a reasonable good faith interpretation of the changes prior to the issuance of final amended regulations.

[9] Section 325 includes a transition rule, providing that the change shall not apply to distributions which are required with respect to years beginning before January 1, 2024, but are permitted to be paid on or after such date.

[10] 89 Fed. Reg. at 58891-2. Section 1.401(a)(9)-2(b)(5).

[11] 89 Fed. Reg. at 58891.

[12] The preamble references the requirements of Code section 411(a)(11). Treasury regulation section 1.411(a)-11(c)(4) provides the following:

Immediately distributable. Participant consent is required for any distribution while it is immediately distributable, i.e., prior to the later of the time a participant has attained normal retirement age (as defined in section 411(a)(8)) or age 62. Once a distribution is no longer immediately distributable, a plan may distribute the benefit in the form of a QJSA in the case of a benefit subject to section 417 or in the normal form in other cases without consent.

[13] Section 1.401(a)(9)-3(c)(5)(3).

[14] Like the proposal, the final rule allows defined benefit plans that have used the regulation's prior definition of age of majority (which refers to whether the child has completed a specified course of education and is under age 26) to retain that definition, provided that the plan adopted that definition on or before February 24, 2022. Section 1.401(a)(9)-6(p)(2)(ii).

[15] In the final regulations, "an example illustrating this rule has been modified to show that the required documentation need not be overly detailed." 89 Fed. Reg. 58893. In addition, the final rule includes transition relief for the documentation deadline in the case of an employee who died in the period from 2020 through 2023.

[16] "[C]onsistent with requests made by commenters, the regulations remove the requirement for a full distribution by the end of the calendar year in which the applicable denominator would have been less than or equal to one if it were determined using the beneficiary's remaining life expectancy (which would have applied in the case of a designated beneficiary who was older than the employee). Accordingly, in the case of an eligible designated beneficiary who was born before the employee, if that beneficiary is taking distributions over the employee's remaining life expectancy, then a full distribution is not required until the calendar year in which the applicable denominator is less than or equal to one." 89 Fed. Reg. at 58897.

[17] See note 6 supra.

[18] However, the final rule adds a new exception (see § 1.401(a)(9)-8(a)) for certain trusts divided upon the death of the employee.

[19] The final regulations provide that an individual who holds an IRA that is an annuity

contract may elect to aggregate the annuity IRA with IRAs that have account balances. § 1.408-8(e)(1)(ii).

[20] Examples of these changes include: the ability to roll over after-tax amounts (basis) to an IRA or plan (if the plan separately accounts for the after-tax amounts); the rule that if only a portion of an eligible rollover distribution is rolled over, the amount rolled over is treated as consisting first of pre-tax amounts; the rule allowing waiver of the 60-day rollover deadline in certain circumstances; and the exclusion of hardship distributions from the definition of an eligible rollover distribution.

[21] In addition, the final regulations clarify that a see-through trust may be treated as a designated beneficiary for purposes of distributions to an inherited IRA held by a non-spouse beneficiary. Section 1.402(c)-2(j)(2)(iii). The final regulations also modify a special rule for certain distributions to surviving spouses (under which a spouse who elects the 10-year rule is required to treat a portion of any annual distribution as an RMD). Section 1.402(c)-2(j)(4). Finally, the final regulations indicate that plan administrators may make reasonable assumptions related to distributions to surviving spouses. Section 1.402(c)-2(j)(4)(vi).

[22] Section 1.402(c)-2 (j)(2)(iv).

[23] The regulations reflect the fact that no RMDs are required from a designated Roth account during the lifetime of the employee.

[24] 89 Fed. Reg. at 58903.

[25] See note 20 supra.

[26] When an individual is the owner of multiple IRAs, the RMD must be calculated separately for each IRA, but the sum of the separately calculated RMDs may be distributed from any of the IRAs.

[27] The regulation incorporates the statutory definition of "correction window," specifying that the correction window ends on the earliest of: (1) the date a notice of deficiency under section 6212 with respect to the tax imposed by section 4974(a) is mailed; (2) the date on which the tax imposed by section 4974(a) is assessed; or (3) the last day of the second taxable year that begins after the end of the taxable year in which the tax under section 4974(a) is imposed. Section 54.4974-1(a)(2)(iii).

[28] The final regulation incorporates the statutory requirement that the corrective distribution must be made from the from the same plan to which the tax relates (in the case of a qualified retirement plan or eligible deferred compensation plan). The regulation clarifies that if the RMD could have been satisfied by a payment from any one of a number of retirement plans (in the case of an IRA or a 403(b) plan), then the corrective distribution may be made from any one of those qualified retirement plans. Section 54.4974-1(a)(2)(iv).

[29] On May 23, 2023, the Chairs and Ranking Members of the House Ways and Means and Senate Finance Committees sent a letter to the Treasury and IRS clarifying congressional intent on various SECURE 2.0 Act items. The letter states that the four Members of Congress intend to introduce technical corrections legislation to correct erroneous statutory language, which may include items not addressed in the letter. For an overview of the letter, see ICI Memorandum No. 35365, dated July 03, 2023, available at https://www.ici.org/memo35365.

[30] The proposal specifies that gift tax method, described in Treas. Reg. section 1.408A-4, Q&A-14(b)(2), should be used.

[31] See text accompanying note 26 supra.

[32] See page 3 of letter.
