INSIGHTS

RETIREMENT STRATEGIES GROUP | AUGUST 2024 LEGISLATIVE UPDATES

Final Regulations for IRAs Inherited under SECURE Act 1.0 Are Here

Designated beneficiaries of inherited IRAs will not be penalized for not taking distributions in prior years. However, beginning in 2025, if the owner died on or after the required beginning date (RBD), designated beneficiaries with inherited IRAs will be required to take annual distributions. This applies to accounts inherited on or after 1/1/20.

The final regulations are here! The key rules are intact, and the at-least-as-rapidly (ALAR) rule is alive and well.

As brief background, the Setting Every Community Up for Retirement Enhancement (SECURE) Act of 2019[1] changed the rules for inherited retirement accounts, including traditional and Roth IRAs. These changes included limiting the stretch period for designated beneficiaries (DBs) to 10 years and creating a new type of beneficiary: the eligible designated beneficiary (EDB). EDBs have the option of using a life-expectancy payout.

Most beneficiaries who inherited qualified accounts in 2020 or later are DBs. DBs are required to liquidate their inherited assets by the end of the year containing the tenth anniversary of the owner's death. The proposed regulations required DBs who inherited an IRA from an owner who died on or after the RBD, to continue to take annual required minimum distributions (RMDs), assuming the separate accounting rules apply. That means that if a deceased owner was taking required distributions, the beneficiary must take them as well.

Recall that when the SECURE Act was issued, most experts interpreted the 10-year rule in the same way as the five-year rule: No need to take an annual RMD—just liquidate the account completely by the fifth (or tenth) year. In February 2022, the proposed regulations from the Treasury provided a very different interpretation: Beneficiaries of accounts were separated based on the account owner's age at death for RMD purposes.

As these are regulations to the existing legislation, they apply from the effective date of the original document—in this case, 2020. In Notices 2022-53, 2023-54, and 2024-35, the IRS waived the penalty for RMDs not taken in years 2021 through 2024. The Coronavirus Aid, Relief, and Economic Security (CARES) Act[2] waived all RMDs in 2020.

The final regulations are clear that DBs who inherited an IRA from an owner who died on or after his or her RBD will need to take an RMD in 2025.

Final Regulations: IRA/Retirement-Account Owner's Age and ALAR

The RBD is the age that a retiree/IRA owner must start taking RMDs. The final regulations retain the provision that treats inherited-IRA distributions based on a pre-or-post RBD date of death. The rule is as follows.

- If the owner had not reached his or her RBD when he or she died, the DB must liquidate the account by December 31 of the year containing the tenth anniversary of the owner's death. Distributions may be taken during the 10-year period but are not required.
- If the owner died on or after his or her RBD, the beneficiary must take annual RMDs in years one through nine using the Single Life Expectancy table (SLE). The account still must be liquidated by the end of the tenth year. This meets the ALAR requirement.

[1]Setting Every Community Up for Retirement Enhancement Act of 2019 (SECURE Act). Employee Benefits Security Administration, Laws & Regulations. Department of Labor.
[2]Coronavirus Aid, Relief, and Economic Security Act (CARES Act), S.3548 — 116th Congress (2019-2020). Congress.gov

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This means that the owner of an inherited IRA where the owner died on or after his or her RBD must take annual distributions starting in 2025. The amount of the distribution is based on the SLE table and the beneficiary's age in the year following the year of death. For example, if the IRA owner died in 2021, the beneficiary would determine the amount using the SLE table and subtract one from that factor for each year since the first required distribution.

Note: If the IRA owner died before 1/1/20 and the primary beneficiary elected life expectancy then subsequently dies, the successor beneficiary has only 10 years to deplete the account.

If the IRA-account owner had not taken his or her RMD in the year of death, the beneficiary can take the RMD. If there are multiple beneficiaries, the year-of-death RMD **can be distributed to one, more than one, or pro rata**. The final RMD for the owner does not count toward the RMD the beneficiary must take, as the beneficiary's obligation to start RMDs begins in the year following death.

Planning Point

While the beneficiary of an inherited account where the owner died after the RBD has the option of taking only the RMD, it may be beneficial to spread the payments over the remaining years more equally. The rule is that the minimum is required, but more can be distributed. Here are two hypothetical examples:

- **Retiring Soon:** A client is two years from retirement, which is when income will drop significantly. The client may want to consider taking the minimum distribution now, then larger distributions within the first two or three years of retirement. This may help reduce the overall tax bill.
- **Retiring Now:** A client ready to retire might consider taking larger distributions from the inherited account so that he/she can delay claiming Social Security retirement benefits or taking distributions from other retirement accounts.

This is an opportunity to meet with clients who have inherited IRAs and help them maximize the income from their important assets based on each client's particular financial needs and goals.

ACTIONS YOU CAN TAKE RIGHT NOW

- **Contact clients who inherited IRAs or qualified accounts on or after 1/1/20.**
- **Review whether or not a distribution is required in 2025.**
- **Help clients evaluate whether or not they should consider adjusting their retirement-income plans based on the final regulations.**

Additional Resources and Links

Internal Revenue Service (IRS), Treasury. "Final Regulations: Required Minimum Distributions."

Notice 2022-53

Notice 2023-54

Notice 2024-35

The SECURE Act: Key Retirement Plan Provisions

For more information about retirement planning, please contact our Retirement Strategies Group at RSG@PacificLife.com or (800) 722-2333, ext. 3939.

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