Traditional, SEP and SIMPLE-IRAs

Understanding Required Distributions

For 2020 and 2021

Questions & Answers

Why are there federal tax rules mandating required minimum distributions from a traditional IRA, SEP-IRA and SIMPLE-IRA?

The primary purpose of a traditional IRA is to allow you and others to save for retirement and then use the funds for retirement and also to accumulate funds for a beneficiary. Therefore, the tax laws require an IRA accountholder to take a required minimum distribution (RMD). After the IRA accountholder dies, the beneficiary or beneficiaries will be required to take required distributions. There are specific formulas for determining how much must be withdrawn, and when. These amounts are called "required minimum distributions" (RMDs).

Congress in 1974 decided that the year a person attains age 70½ is a reasonable time to require a person to commence withdrawals from his or her traditional IRA, SEP-IRA or SIMPLE IRA.

Congress and President Trump decided in December of 2019 that the age 70½ requirement should be changed to age 72. One reason for this change is that IRA owners are generally living a little longer.

What two new laws impact a person's RMD for 2019 and 2020?

<u>Due to COVID-19, the CARES Act waives the 2020 RMD for each IRA accountholder and each IRA beneficiary.</u> In order to assist during these hard economic times, a person is not required to take a 2020 RMD, include it in income and pay the associated taxes. The CARES Act (Coronavirus Aid, Relief and Economic Security Act) was signed into law by President Trump on March 27, 2020.

On December 20, 2019, President Trump signed into law the SECURE Act which changed the age a person becomes subject to the RMD rules to age 72 from age 70½.

When does the new age 72 rule become effective?

Due to the waiver, it becomes effective for 2021. Any person attaining age 72 in 2021 will be required to take an RMD for 2021. The person's required beginning date is April 1, 2022. A person who attained age 72 prior to 2021 is also required to take an RMD for 2021.

If I was distributed my RMD prior to March 27, 2020, or soon thereafter, was I eligible to rollover this distribution?

In general, yes. You needed to comply with the IRS guidance furnished in Notice 2020-23 and Notice 2020-51. In general, you had to complete your rollover by August 31, 2020.

What happens if I fail to withdraw the required minimum distribution?

Current federal income tax law provides a penalty tax of 50% of the amount required to be distributed, but which was not. For example, if you failed to withdraw a required minimum distribution of $1,000 for a given year, then you owe a tax of $500.

What are the tax consequences of receiving an RMD?

The general taxation rule for traditional IRAs will apply. A recipient (you or your beneficiary) will include the amount received in gross income for the year of receipt. You (or your beneficiary, if applicable) will pay taxes with respect to this amount at the marginal income tax rate which applies to you (or your beneficiary if appliable), unless a portion of the distribution is not taxable because it is comprised of basis.

Must I withdraw all of my money because I am 72, or may I withdraw IRA funds over a number of years?

You are <u>not</u> required to withdraw all of your IRA funds in one year. You are permitted to set up a distribution schedule over a number of years, as long as you take each year your RMD amount or a larger amount.

As long as your money is in your IRA, it remains tax deferred, as do any earnings. By using periodic payments over a number of years, you spread your income out over the Payment schedule and typically will pay less tax.

How is my required minimum distribution calculated under the RMD rules ?

The balance of your IRA as of the preceding 12/31 is divided by the divisor from the Uniform Lifetime Table, based on the age of the accountholder. For example: the fair market value of your IRA as of 12/31/20 is $15,000. Your age is 77 in 2021. The divisor from the Uniform Lifetime Table is 21.2. Your required minimum distribution for 2021 is $15,000/21.2, or $707.55.

Formula #1 RMD $= \dfrac{\text{Account Balance as of Preceding 12/31}}{\text{Period from Uniform Lifetime Table}}$

Formula #2 RMD $= \dfrac{\text{Account Balance}}{\text{Period from Joint Lives Table}}$

What is the Uniform Lifetime Table?

It is the table which the IRS has instructed be used for determining the distribution period for lifetime distributions to an IRA accountholder when his or her spouse is either not the sole designated beneficiary, or is the sole beneficiary, but is not more than 10 years younger than the accountholder.

Uniform Lifetime Table

Age of IRA Account-holder	Distribution Period (in years)	Age of IRA Account-holder	Distribution Period (in years)	Age of IRA Account-holder	Distribution Period (in years)
72	25.6	87	13.4	102	5.5
73	24.7	88	12.7	103	5.2
74	23.8	89	12.0	104	4.9
75	22.9	90	11.4	105	4.5
76	22.0	91	10.8	106	4.2
77	21.2	92	10.2	107	3.9
78	20.3	93	9.6	108	3.7
79	19.5	94	9.1	109	3.4
80	18.7	95	8.6	110	3.1
81	17.9	96	8.1	111	2.9
82	17.1	97	7.6	112	2.6
83	16.3	98	7.1	113	2.4
84	15.5	99	6.7	114	2.1
85	14.8	100	6.3	115	1.9
86	14.1	101	5.9		

Note. In November of 2020 the IRS issued a final regulations setting forth an updated Uniform Lifetime Table which will be used to calculate RMDs for 2022 and subsequent years. The Uniform Lifetime Table as created by the IRS in 2002 will still be used for 2021 RMD calculations.

Does it make much difference for RMD purposes who my IRA beneficiary is?

No. The Uniform Lifetime Table is used to determine the divisor regardless of who is your IRA beneficiary. There is one exception. The Joint Life Expectancy Table is to be used when the IRA owner has designated his or her spouse to be the sole primary beneficiary and such spouse is more than 10 years younger.

If I attain age 72 in 2021, what is my deadline to withdraw such RMD?

Your deadline is your required beginning date.

What is my required beginning date?

Your required beginning date is April 1 of the year following the year in which you reach age 72.

What "age" is used to determine the distribution period (i.e. life-expectancy factor) for the first year?

Age 72 is used.

If my first distribution has to be withdrawn by April 1 of the year after the year I reach age 72, when do I have to take additional distributions? What is my deadline for these distributions?

You are required to take distributions for each calendar year after the year you reach age 72. While you have until April 1 of the year after the year in which you turn age 72 to take your first distribution, distributions for the second year must be made by December 31 of such year. The deadline for subsequent distributions is December 31 of each subsequent year.

May I withdraw more than my required minimum distribution?

Yes.

Must the distribution schedule I establish also be the same as my required minimum distribution schedule?

No. The rule is that the amount distributed each year must always equal or exceed your RMD amount for such year.

What is the IRA custodian's role with respect to RMDs?

Every IRA custodian/trustee must furnish an RMD notice to each IRA accountholder who must take a required distribution for a given year. For example, if an accountholder is required to take an RMD with respect to 2021, then the IRA custodian must furnish the notice by January 31, 2021. The IRA custodian has the following two options for furnishing this notice: (1) to calculate your RMD for you, or (2) to simply notify you of your RMD requirement, and calculate the amount and provide it to you only if requested. The IRA custodian may choose to inform you that you do not need to take a distribution from the specific IRA as long as you use the alternative certification method and take the RMD amount for that IRA from another IRA. The IRA custodian must also inform you of the date by which such amount must be distributed, and that the IRS is being informed each year, on the Form 5498, that you must take an RMD.

Is my IRA custodian required to give the IRS any information about my RMD?

Yes. The IRA custodian must, on an annual basis, indicate on the Form 5498 if an RMD is required with respect to the related IRA. At the present time, the IRS and Congress do not require that a person's actual RMD amount be reported to the IRS.

Is there a worksheet which I may use to calculate my required minimum distribution?

Yes, an RMD worksheet is provided later in this brochure.

What rules apply if I wish to roll over funds from an IRA to a different IRA? Are there any special RMD rules with which I must comply?

Yes. The rules applying to rollovers have not changed. A person is ineligible to roll over an RMD. If one does, then it will be an excess contribution.

The IRS rules provide that the first money out of your IRA for a given year is defined to be your required distribution for such year, until your requirement is met. Therefore, if you were to take a distribution early in the year, thinking you could roll it over and later take your RMD amount, the IRS would consider the distribution to be part of your RMD amount, and rolling over an RMD amount is not permissible. You may, of course, use the alternative certification method and take your RMD amount for one IRA from a different IRA.

What rules apply if I wish to transfer funds from an IRA to a different IRA?

Current tax rules allow you to transfer your entire IRA balance (including any RMD for such year) from one IRA to another IRA. You must understand that there are some risks associated with this rule.

The rules clearly state that the two IRA custodians (i.e. sending and receiving) are not responsible to redetermine your RMD amount just because you transfer funds out of their IRA or transfer funds into their IRA. This means that you, the accountholder, will be responsible to make sure that you withdraw your RMD from wherever you wish.

Do all distributions count towards satisfying the RMD amount?

Almost all distributions do count; even the distribution of nondeductible contributions are counted. However, "corrective distributions" pursuant to Code section 408(d)(4), 408(d)(5), 408(k)(6)(C) or similar items defined by the IRS commissioner do not reduce the RMD amount.

What withholding rules will apply to the periodic distributions made to me?

Prior to commencing your periodic distributions, you will need to instruct the IRA custodian whether or not you want to have federal income tax withheld from your distributions. Your IRA custodian will furnish you the necessary form. You may instruct the IRA custodian to withhold 10% of your distributions, an additional amount in excess of the 10%, or not to have withholding. You must be aware that there are penalties for not paying sufficient tax during the year, either through withholding or estimated tax payments. The IRS advises new retirees to review Publication 505. It explains your estimated tax requirements and describes penalties in detail.

Am I required to take a minimum distribution from each IRA I have?

No. The minimum distribution amount must be calculated separately for each IRA you have. Under the final RMD rules, the IRA custodian must determine your RMD if you request it. However, you do not have to take a distribution from each IRA, as long as you satisfy the total minimum distribution amount from at least one IRA.

Example: Roberta is age 76 (distribution period of 22.0) in 2020, and she has four IRAs at four different IRA custodians:

IRA Custodian	IRA Balance	RMD Amount
First Bank	$5,000.00	$227.27
First Brokerage	$15,000.00	$681.82
Second Bank	$30,000.00	$1,363.64
Second Brokerage	$20,000.00	$909.09
Aggregate RMD TOTAL		$3,181.82

Roberta can take the $3,181.82 from the first IRA, the second IRA, the third IRA, the fourth IRA or in any combination, as long as she satisfies her required minimum distribution of $3,181.82. If Roberta withdraws $3,181.82 from the IRA at First Bank, then she should inform the other three custodians in writing that she has satisfied her RMD requirement by withdrawing funds from the IRA at First Bank.

Traditional IRAs, Roth IRAs, 401(k) plans, and 403(b) plans are four different types, so these may not be aggregated. This special aggregation rule does not apply to distributions from Qualified Plans. There must be a separate distribution from each qualified plan, and a distribution from an IRA can not be used to satisfy an RMD for a QP, or vice versa.

The IRS in adopting the final regulation modified the rule so that only the RMDs of "like-kind" IRAs may be aggregated for purposes of this special distribution rule.

Examples of "like-kind" IRAs:

1. Traditional IRAs of a person who holds them as an accountholder;
2. Traditional IRAs of a person who holds them as a beneficiary, as long as related to the same deceased IRA accountholder (i.e. an inherited IRA); and
3. Roth IRAs of a person who holds them as a beneficiary of the same deceased Roth IRA accountholder (i.e. an inherited Roth IRA).

   For RMD purpose, a standard traditional IRA, SEP-IRA and SIMPLE-IRA are all defined to be traditional IRAs.

A distribution from an IRA which is not of the same type may not be used to satisfy the RMD requirement of another type of IRA.

If my RMD may be calculated using the Joint Life and Last Survivor Expectancy Table, where can I find it and what divisor will apply to me?

You are eligible to use the Joint Life Table (JLT) if your spouse is your sole beneficiary and he or she is more than 10 years younger than you. The divisor or number applying to you from the JLT is larger than the number found in the Uniform Lifetime Table (ULT). This means your RMD will be smaller than if determined by using the number from ULT. An IRA custodian is allowed to calculate your RMD using the ULT even though you qualify to use the JLT. Annually you may refer to Appendix B of IRS Publication 590-B (IRA Distributions) to determine your divisor. You use your age and the age of your spouse. The IRS will be issuing a new JLT and ULT to be used for 2022 RMD calculations.

What happens if there is a change in my marital status after January 1?

There is no change in your RMD calculation if your beneficiary is not your spouse.

If your spouse is your sole beneficiary as of January 1 and your spouse would die after January 1, or you become divorced after January 1, you will still be treated as married for such year. However, you would not qualify to use the Joint Table for subsequent years unless you would remarry and qualify again under the special rule.

What happens if I designate a beneficiary other than or in addition to my spouse during the current distribution calendar year?

If your spouse is not your sole beneficiary or he or she is not more than 10 years younger than you, there will be no effect on your RMD for the current year.

If your spouse is your sole beneficiary and he or she is more than 10 years younger than you, then your RMD amount will need to be redetermined by using the Uniform Lifetime Table. Your RMD would increase.

Will I be able to use a tax-free charitable distribution to satisfy my required distribution?

Yes, the general rule is, the IRS has issued guidance that a person who has made a QCD may also use that amount to satisfy their RMD. The SECURE Act requires a person to lower the amount they are entitled to treat as a QCD by the amount of their deductible annual traditional IRA contributions. The IRS will need to furnish guidance how this new law impacts a person's required distributions. Presumably, if a person is unable to exclude an amount as a QCD, then the person cannot use such amount to satisfy their RMD requirement.

Can you give an example of what tax benefit I would receive by making a tax-free charitable distribution for 2021?

Yes. Let's assume that you normally give your church $900 each year. Your required distribution amount was $800. If you will instruct your IRA custodian to withdraw $900 from your IRA and directly pay it to your church, then you will not be taxed on this distribution.

Once I die, are there required distribution rules applying to my beneficiary(ies)?

Yes. Other CWF brochures (#154 and #156) devoted to this topic. You may also review IRS Publication 590-B. There are rules requiring your beneficiary(ies) to withdraw certain minimum distributions by various deadlines. If such distributions do not occur by the appropriate deadline, then your beneficiary will owe the 50% excise tax. Some IRA plan agreements may require you to inform your beneficiary(ies) that he or she is a beneficiary of your IRA. The rules as to when and how much must be withdrawn by your beneficiary(ies) will depend on whether the beneficiary is an eligible designated beneficiary (EDB) or not. If the beneficiary is not an EDB, then the general rule is that the inherited IRA must be closed by December 31 of the year containing the 10th anniversary of the IRA owner's death. The rules applying to a beneficiary will not apply to your spouse if he or she is your sole primary beneficiary and he or she elects to treat your IRA as his or her own IRA. In this case, your spouse will not be required to start withdrawing funds until he or she becomes subject to the required distribution rules as an IRA accountholder.

RMD Worksheet

1. Value of IRA as of 12-31 (of previous year). ___________ (1)
2. Add in outstanding rollovers, transfers. ___________ (2)
3. Adjusted account balance to be used (line (1) plus line (2)). ___________ (3)
4. Your age as of 12-31 of current year. ___________ (4)
5. Determine the life-expectancy factor. ___________ (5)
   (Use the applicable Table.)
6. Divide the amount on line (3) by the number listed on line (5). ___________ (6)
   (This is the amount of the required minimum distribution before any distributions are credited.)