IRS Finalizes (and Proposes Additional) Updates to Required Minimum Distribution Rules

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On July 19, the IRS issued both final and proposed regulations to address the complex rules that apply when members (and their beneficiaries) need to take a distribution from their qualified plan – called required minimum distributions ("RMDs"). The RMD regulations apply to both governmental and ERISA covered plans. This Q&A summary focuses on how the final regulations impact governmental defined contribution plans (including 403(b) plans).

When are these regulations effective?

The final regulations are effective for distributions for calendar years beginning on and after January 1, 2025. For prior distributions, all plan sponsors must apply the pre-existing final regulations, taking into account reasonable, good faith interpretations of the changes made under SECURE 1.0 and SECURE 2.0 (as applicable to distributions with respect to members who die after December 31, 2021 for governmental plans). Importantly, for governmental plans, the Pension Protection Act rule allowing governmental plans to use a "reasonable and good faith standard" for compliance with the RMD rules continues to apply on and after 2025.

When must benefits commence to a member?

The IRS requires 401(a), 401(k), 403(b) and 457(b) plans to commence paying benefits when a member reaches his or her required beginning date. That date now varies depending on the member's birthdate, as set forth in the table below. The proposed regulations provide that for those born in 1959, the applicable age is 73, consistent with the legislative history, clearing up the confusion caused by the statutory language. Otherwise, the historic RMD rules for payments during a member's lifetime generally continue to apply (except that following SECURE 2.0, designated Roth accounts in 401(k), 403(b) and 457(b) plans are no longer subject to these rules and therefore are not taken into account in determining the amount of the RMD payment).

Birthdate	Required Beginning Date
Before July 1, 1949	70½
July 1, 1949 – December 31, 1950	72
January 1, 1951- December 31, 1959	73
January 1, 1960 and after	75

When must benefits commence to a beneficiary?

It depends on the type of beneficiary, whether plan benefits have commenced, and the plan terms, but in general:

- ***Eligible Designated Beneficiary*** (surviving spouse, minor child (under age 21), chronically ill or disabled (or certain trusts for same), or other older individual (or no more than 10 years younger than the member))[1] -
    - Member dies before reaching his or her required beginning date: The beneficiary can elect to receive payments over their lifetime, and if payments remain due after the beneficiary's death, all payments from the account must be paid out no later than the end of the calendar year that includes the 10th anniversary of the beneficiary's death. Except for certain payments to surviving spouses, lifetime payments must begin in the year following the member's death. Alternatively, the beneficiary may elect the 10-year rule – that is payments must be made by the end of the calendar year that includes the 10th anniversary of the member's death.
    - Member dies on or after reaching their required beginning date: Payments must continue under the "at least as rapidly" rule – so annual payments continue over the longer of the beneficiary's life expectancy or the member's remaining life expectancy.
- ***Designated Beneficiary*** (an individual who is not an eligible designated beneficiary and certain trusts) -
    - Member dies before reaching their required beginning date: The beneficiary (including any successor beneficiaries) must receive the entire account by the end of the calendar year that includes the 10th anniversary of the member's death. No payments are required for years 1-9.
    - Member dies on or after reaching their required beginning date: The beneficiary (including any successor beneficiaries) must receive the entire account by the end of the calendar year that includes the 10th anniversary of the member's death, plus annual payments must be made under the "at least as rapidly" rule – so annual payments are required for all of years 1-10. Transition relief was provided through 2024, but these payments will be required beginning in 2025.
- ***Nondesignated Beneficiary*** (estate, charity, certain trusts) –
    - Member dies before reaching their required beginning date: The beneficiary must receive the entire account by the end of the calendar year that includes the 5th anniversary of the member's death.
    - Member dies on or after reaching their required beginning date: The beneficiary must receive annual payments over the remaining lifetime of the member.

What happens if these RMD payments are not made timely?

There is a 25% excise tax (down from the historic 50% excise tax) on the member (or beneficiary) for amounts that are not timely paid out, and there may be plan qualification concerns for failure to comply with these regulations. SECURE 2.0 provides that this 25% rate can be lowered to 10% if certain correction steps are taken by the member/beneficiary.

When are plan amendments required?

These regulations do not extend the deadline for plan amendments to reflect these changes, which are currently due by December 31, 2029 for governmental plans. Notably, some model amendment language for defined contribution plans is available – see https://www.irs.gov/pub/irs-tege/dc-lrm0124.pdf (item #49).

[1] There are also special rules for certain spouses who can elect to be treated as the member under the new proposed regulations, and special rules for a minor child under the final regulations.

What special rules apply to 403(b) plans?

403(b) plans generally track the traditional IRA rules for determining RMD payments (which largely mirror the rules outlined above), although the rules for Roth accounts follow the defined contribution plan rules. The IRS is considering if further changes are desired to conform the rules for these plans to the 401(a), 401(k) and 457(b) defined contribution plan RMD rules (rather than continuing the closer conformity to the special IRA RMD rules) and may issue separate guidance on this issue. One issue under consideration is the elimination of the rule that currently allows members to choose which 403(b) contract will satisfy the aggregate RMD requirement, but that rule was not changed in the final regulations. For some 403(b) plans, realigning the 403(b) plan RMD rules with the rules for other plans could cause significant operational changes and/or concerns.

What actions steps should I take now that these regulations have been issued?

Governmental plans should review the new final regulations with their internal or external recordkeeper/administrator and see what, if any, changes are necessary to comply with these final regulations. The final regulations closely track the 2022 proposed regulations, but some technical changes were made, like removal of the special rule for older beneficiaries and changes to the spousal IRA rollover option.

Also, stay tuned for additional SECURE 2.0 rules that are set forth under the new proposed regulations and that are intended to provide additional guidance on certain key SECURE changes, including the spousal election and Roth account treatment. RMD provisions impact not just the plan's distribution polices and forms, but also Form 1099-R reporting and withholding, and rollover treatment, all of which need to be coordinated.