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SECURE, CARES acts change rules on required minimum distributions

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In this article
Increase in age for RMDs | New RMD rules for distributions from DC plans after death | CARES Act suspends DC plan RMDs for 2020 | Guidance for 2020 RMD notifications/distributions made in error | Plan amendments required | Related resources

The Setting Every Community Up for Retirement Enhancement (SECURE) Act, enacted Dec. 20, 2019, as part of a government spending package (Pub. L. No. 116-94), increases the age at which required minimum distributions (RMDs) must begin. The law also largely eliminates "stretch" distributions to beneficiaries of defined contribution (DC) plans. Just over three months later, enactment of the Coronavirus Aid, Relief, and Economic Security (CARES) Act (Pub. L. No. 116-136) waives most RMDs from DC plans for 2020. Although these changes also affect individual retirement account (IRA) holders, this article focuses on the impact on employer-sponsored plans.

Increase in age for RMDs

Under Internal Revenue Code (IRC) Section 401(a)(9), participants in employer-sponsored DC and defined benefit (DB) plans — including all qualified, 403(b) and governmental 457(b) plans — must begin receiving RMDs by the required beginning date (RBD).

Plan vs. statutory RBD. The RBD is the latest date to which a plan can let a participant defer starting distributions. But retirement plans may also force payments to start earlier at any time on or after the participant reaches normal retirement age (usually age 65). A plan with an earlier starting date may refer to that date as the RBD. However, for purposes of this article, RBD refers only to the statutory date, not any earlier date used by the plan.

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Statutory changes in RBD

The Tax Reform Act of 1986 (TRA ’86) defined the RBD as April 1 of the year after the year in which a participant turns age 70-1/2, even if the participant is still working. However, the Small Business Job Protection Act (SBJPA) of 1996 amended the definition of RBD to delay it until April 1 after the year of retirement for participants (other than 5% owners) who work past age 70-1/2. This definition of RBD remained in effect until Congress passed the SECURE Act.

The SECURE Act increases the RBD triggering age from 70-1/2 to 72. Accordingly, the new RBD is April 1 after the year a participant reaches age 72 or retires, whichever is later. The RBD change applies to participants who turn 70-1/2 after Dec. 31, 2019 (that is, have birthdays on or after July 1, 1949). The SECURE Act’s changes don’t affect individuals who turned 70-1/2 before 2020. But as discussed later, the CARES Act waives RMDs that would otherwise be payable in 2020 for participants in DC plans or IRAs (see “CARES Act suspends DC plan RMDs for 2020”).

Special rules for 5% owners. The SBJPA change extending the RBD triggering age for participants working past 70-1/2 did not apply to employees who were 5% owners. Their RBD remained April 1 after the year they turned 70-1/2, even if still employed. The SECURE Act changes the triggering age from 70-1/2 to 72 for 5% owners, but their payments still must start even if they continue working. The remainder of this article assumes that participants are not 5% owners.

Is the new RBD mandatory or optional?

Some employers might not want to adopt the SECURE Act’s changes — for instance, if the employer’s plan provides very generous actuarial increases for participants who work after age 65. These employers should be able to retain their plans’ existing provisions. After the SBJPA’s enactment, IRS regulations made clear that plans could continue to use the TRA ’86 rules. IRS will need to update the 401(a)(9) regulations for the SECURE Act’s changes. But if the existing 401(a)(9) regulations are a guide, then employers presumably have the same flexibility to use a 70-1/2 triggering age, despite the SECURE Act’s changes.

Statutory RBD applies for rollover eligibility. A distribution isn’t eligible for tax-favored rollover treatment to the extent the distribution is required under 401(a)(9). So for rollover purposes, the statutory definition of RBD applies — not the plan’s definition, if different from the 401(a)(9) definition.

Before the SECURE Act, if a plan used the SBJPA’s RBD definition, then a portion of any distribution made on that RBD was a required distribution under both the terms of the plan and 401(a)(9). (Briefly, the required distribution is equal to an annuity payment; amounts above the annuity payment aren’t required distributions.) The required portion of the distribution therefore was ineligible for rollover treatment.

After the SECURE Act, if a plan doesn't adopt 72 as the triggering age, payments made before the RBD are no longer required distributions under 401(a)(9). As a result, these payments are eligible for rollover in their entirety (if they otherwise meet the Code's definition of "eligible rollover distribution").

> Example. A plan requires participants to start payment on April 1 after the year a participant attains age 70-1/2 or, if later, the year the participant retires. The plan sponsor doesn't change the triggering age after the SECURE Act. A participant turns 70-1/2 on Sept. 5, 2021, and retires on Dec. 1 of that year. Under the plan's terms, the participant must start receiving benefits on April 1, 2022. The participant elects a lump sum. The entire distribution on that date is eligible for tax-favored rollover treatment because no portion of the distribution is required under Section 401(a)(9) as amended by the SECURE Act.

DB actuarial increases unchanged

Section 401(a)(9)(C)(iii) requires an actuarial adjustment for DB plan benefits paid when a participant retires in a calendar year after attaining age 70-1/2. The SECURE Act doesn't change this section of the Code, so the result initially seems clear: DB participants who retire after 70-1/2 will get actuarial increases on their accrued benefits from that age, even if they retire before the new RBD.

The Joint Committee on Taxation and House Ways and Means Committee reports on the SECURE Act confirm that this is what Congress intended. But a close reading of the statute could lead to a different conclusion. As currently written, the provision requires an actuarial increase only when a participant's RBD is delayed until April 1 after the year of retirement. This implies that a participant who retires at age 71 is now ineligible for an actuarial increase because the RBD has not been delayed — even though that individual would have received an increase under the old law. Informal comments from IRS representatives indicate this detail will likely be fixed through a technical correction.

Impact may be limited

The RBD change should have a limited impact on plan operations for many employers. Employers choosing to retain their plans' existing payment provisions need to ensure that benefits paid before the RBD are treated as rollover-eligible (as applicable), but should otherwise be unaffected. Plans that don't force payments to start while participants are working should see only small changes in operations, even if the employer changes the triggering age to 72.

The largest operational impact may be on plans that maintained the TRA '86 definition but take this opportunity to delay the payment date until April 1 of the year after a participant turns age 72 or later retires. Making this change eliminates an in-service distribution option and would ordinarily be prohibited by the anti-cutback rules of Section 411(d)(6). However, the SECURE Act includes broad anti-cutback relief (see "Plan amendments required" below). Employers can now eliminate the age 70-1/2 distribution option and either replace it with a later one or make participants wait until retirement to receive their first distribution. These employers also need to provide actuarial increases starting at 70-1/2, though none may have been required before (if the plan suspended benefits after the normal retirement date).

New RMD rules for distributions from DC plans after death

The SECURE Act changes the way DC plans pay RMDs after a participant's death. Before the SECURE Act, the distribution of a deceased participant's unpaid benefits generally could be stretched out over the life expectancy of the participant's beneficiary. After the SECURE Act, these stretch payments can be made only to an "eligible designated beneficiary." Other beneficiaries must receive all remaining benefits within 10 years of the participant's death.

Eligible designated beneficiary

Eligible designated beneficiaries are:

- The participant's surviving spouse
- The participant's minor child
- A permanently disabled individual
- A chronically ill individual
- An individual who is not more than 10 years younger than the participant

Limitations on stretch period

Although the SECURE Act allows an eligible designated beneficiary to stretch RMDs over the beneficiary's lifetime, some limitations apply:

- Minor child who reaches age of majority. Minor children cease being eligible designated beneficiaries when they reach the age of majority. At that point, any remaining benefits must be paid to the child within 10 years.
- Death of eligible designated beneficiary. If the eligible beneficiary dies, any remaining benefits must be distributed within 10 years.

Exceptions for other beneficiaries

Designated beneficiaries — that is, beneficiaries who are not eligible designated beneficiaries — generally must receive their payments over 10 years. But three exceptions apply:

- If a participant died before Jan. 1, 2020, distributions can continue to be made over the beneficiary's lifetime. But upon the beneficiary's death, the remaining account balance must be distributed within 10 years.
- The new rule does not apply to "qualified annuities" — binding commercial annuity contracts in effect on Dec. 20, 2019 (the date the act was signed into law) that satisfy two conditions:
  - The contract makes payments over the life of the participant or over the joint lives of the participant and a designated beneficiary.
  - The participant made an irrevocable election before Dec. 20, 2019, as to the method and amount of the annuity payments (whether or not payments had started by that date).

Beneficiary is an entity. Before the SECURE Act, a special rule applied when the beneficiary was the deceased participant's estate or another entity, such as a charitable organization or trust. For these beneficiaries, the participant's unpaid account balance had to be distributed within five years after the participant's death. The SECURE Act made no change to this rule, so these payments are still subject to the five-year rule.

Effective date

The new rule for DC plan distributions after death applies to beneficiaries of participants who die after Dec. 31, 2019, except as follows:

- For governmental plans, the new rule applies to beneficiaries of participants who die after Dec. 31, 2021.
- For collectively bargained plans, the new rule applies to beneficiaries of participants who die after Dec. 31, 2019, or, if later, the date on which the last collective bargaining agreement terminates, but no later than Dec. 31, 2021.

CARES Act suspends DC plan RMDs for 2020

The SECURE Act's RMD changes don't affect individuals who turned 70-1/2 during 2019: Their RBD doesn't change. In a similar manner, individuals who reached their RBD before 2019 and are currently taking RMDs must continue to do so, even if they are not yet 72.

But the CARES Act grants a one-year waiver for RMDs otherwise payable in 2020 from DC plans or IRAs. (The waiver does not apply to DB plans.) This waiver applies to all RMDs from these plans, including distributions for participants who turned 70-1/2 in 2019 and would ordinarily have received two distributions in 2020 — one in April for 2019 and another by year-end for 2020. Participants whose RMDs began before 2020 also get the one-year waiver. This is a waiver, not a delay; participants will not have to take extra distributions in 2021 to make up for distributions waived in 2020.

Eligible rollovers. Any distributions in 2020 that would have been RMDs absent the waiver can be rolled over to another employer plan that accepts rollovers or to an IRA. However, some exceptions to the usual rollover rules apply:

- The distributing plan doesn't have to make a direct trustee-to-trustee transfer.
- The mandatory 20% withholding on eligible rollover distributions doesn't apply.
- The employer doesn't need to provide a 402(f) rollover notice.

Guidance for 2020 RMD notifications/distributions made in error

In Notice 2020-6, IRS granted relief to financial institutions who had mistakenly sent certain required notices to individuals who would have needed to take an RMD from their IRA in 2020, but whose RBD changed after the SECURE Act. To qualify for the relief, the financial institution needs to notify the IRA owner of the error by April 15.

Employer-sponsored plans do not need to provide such notification. But Notice 2020-6 says IRS is considering providing additional guidance for plan administrators, payers and distributees if a distribution made to an individual who will turn 70-1/2 in 2020 was treated as an RMD. The need for this guidance is more critical now that the CARES Act has suspended all RMDs for DC plans and IRAs — effective merely five days before initial RMD payments for 2019 were due.

Plan amendments required

Plans will have to be amended to reflect the new 401(a)(9) rules. The SECURE Act's RBD changes generally require an amendment, regardless of whether the plan maintains or changes its existing payment provisions. Plans will also need amendments to reflect the SECURE Act's new provisions for distributions after death and the CARES Act's waiver of 2020 RMDs.

Plan amendments for both the SECURE Act and the CARES Act won't be due before the last day of the first plan year beginning on or after Jan. 1, 2022 (or a later date prescribed by IRS). Although IRS provided model amendments after issuing the existing 401(a)(9) regulations, the agency has yet to indicate if it will do so for the SECURE Act's changes. But since curtailing the determination letter program for individually designed plans, IRS has said that it may use model amendments to help employers comply with changed requirements for qualified plan documents.

Anti-cutback relief. Both the SECURE Act and the CARES Act provide anti-cutback relief for the changes to the 401(a)(9) rules. The SECURE Act's broad anti-cutback relief applies to any plan amendment reflecting the statute's changes for employer-sponsored plans. The relief covers required amendments to comply with the SECURE Act, as well as discretionary amendments adopting the law's optional provisions. The CARES Act provides anti-cutback relief for waived RMDs in 2020. For both changes, employers must adopt conforming amendments by the plan amendment deadline in order to receive the anti-cutback relief.

Related resources

Non-Mercer resources

- Pub. L. No. 116-136, the CARES Act (Congress, March 27, 2020)
- Section-by-section summary of the CARES Act (Senate Health, Education, Labor & Pensions Committee, March 25, 2020)
- Notice 2020-6 (IRS, Jan. 24, 2020)
- Division O of Pub. L. No. 116-94, the SECURE Act (Congress, Dec. 20, 2019)

Mercer Law & Policy resources

- Stimulus bill gives 2020 DB funding relief, access to DC savings (March 26, 2020)
- SECURE Act set to become law (Dec. 19, 2019)
- IRS plans to update mortality tables for required minimum distributions (Nov. 18, 2019)

Other Mercer resources

- Stay informed on the coronavirus (regularly updated)

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