Understanding lifetime RMD rules for IRAs, qualified plans and annuities

In brief

Most clients nearing retirement have a basket of assets to provide retirement income. The basket could include traditional IRAs, SEP and SIMPLE IRAs, qualified plans, 403(b) accounts, and annuities (both inside IRAs and qualified plans). While these types of accounts provide benefits for individuals saving for retirement (like tax-deferred growth), they require the client to take annual minimum distributions (Required Minimum Distributions, or RMDs) once an individual reaches his or her required beginning date (age 72, 73, or 75 depending on year of birth). If a client was age 72 in 2022, they had an RMD requirement in that year and continue to have that annual requirement going forward. If a client was age 71 in 2022, they don't have their first RMD until 2024. Age 75 will be the new RMD age in either 2033 or 2034, dependent on corrective legislation or guidance from the Treasury Department.

Which table does the client use to calculate their RMD from their tax favored retirement account?

IRS Publication 590-B provides three tables to choose from when determining the client's life expectancy and the factor used to determine their RMD for the year. These tables apply to all IRAs and retirement accounts.

Uniform Life Table

Most retirement account owners use this table while they are alive, whether they are single or married.

Joint and Last Survivor Table

Account owners use this table if their spouse is more than ten years younger and is the sole beneficiary of their account.

Single Life Expectancy Table

This table is used if the client inherited a retirement account.

How does the client determine their RMD for the year?

The December 31 account balance from the prior year is divided by the client's life expectancy factor found in one of the tables above (based on the age they will turn in that calendar year). See examples on page 5 for instructions on how to calculate the RMD using the Uniform Lifetime Table.

If the client owns multiple IRAs, qualified plans or 403(b) accounts, do they have to take an RMD from each account?

If the client owns multiple IRAs (including SEPs, SIMPLEs, or IRA deferred annuities), they must calculate the RMD for each IRA, but they can satisfy the total RMD for IRAs from one or more of those IRAs.[1]

If the client owns multiple (non-IRA based) qualified plan accounts, they must calculate their RMD for each account and must take that RMD from each account (they can't aggregate RMDs from one qualified plan account the way they can with IRAs). In addition, they can't take RMDs from IRAs to satisfy the qualified plan RMD or vice versa.

TYPES OF ACCOUNTS LIFETIME RMD RULES APPLY TO

- Traditional IRAs
- SEP and SIMPLE IRAs
- 401(k) or profit-sharing plans
- 403(b) plans
- 457(b) plans

How is the client's account balance determined for RMD purposes if they own an annuity inside a tax favored retirement account?

When an immediate annuity is purchased inside a retirement account, special transition rules apply that affect the RMD requirements in the year of purchase and when payouts begin. In general, if the client has a deferred annuity inside a retirement account, they must value the annuity each year and include the value in their year-end account balance to calculate your RMD.[2] This is relatively straightforward with a variable annuity or fixed deferred annuity, as those contracts usually have a readily available market value.

However, if they purchase an immediate annuity or annuitize a deferred annuity inside a retirement account after the required beginning date, they still must take an RMD based on the prior year-end account balance for the year they buy the immediate annuity or annuitize an annuity. Because of this rule, it's usually a good idea for the client to take their full RMD prior to the purchase or annuitization. Under Secure Act 2.0, for IRAs (SEP, SIMPLE, Traditional) the client can elect to count annuitized annuity payments towards RMD requirements in the year of purchase or for future years for aggregating RMDs among IRAs. The IRS has not issued any guidance as to how a taxpayer can aggregate payments from annuitized IRAs contracts with deferred IRAs for RMD calculations.

What happens if the client fails to take the RMD by the required deadline?

If the client fails to take their full RMD by December 31 of the year in question, then they generally must complete IRS Form 5329 (Additional Taxes on Qualified Plans and IRAs) and pay either a 25% or 10% penalty on the excess accumulations due to insufficient distributions.

Note that for most people, the first RMD for deferred IRAs does not have to occur until April 1 of the year following the year in which they reach age 72, 73, or 75 depending on their year of birth. If a client waits until April 1st of the following year, they must take two RMDs that year; one for the year they reach the required age, and the following year. However, December 31 is the deadline for every year after the first year.

The chart on the following pages summarizes the lifetime RMD rules.

[1] Treas. Reg. § 1.408-8, Q-9

[2] Treas. Reg. § 1.401(a)(9)-5

Required Minimum Distribution Chart

GROUPING FOR AGGREGATION RULE	MARKET PLAN TYPE	AVAILABLE PRODUCTS	RMD DUE DATE AND CALCULATION	NOTES AND EXCEPTIONS
GROUP 1 IRA-Based Accounts can be aggregated and RMD paid out of single account. Inherited IRAs can only be combined with other inherited IRAs from same decedent.	Traditional IRA SEP IRA SIMPLE IRA Inherited IRAs	Brokerage and Advisory Accounts Variable Deferred Annuities (VA) Fixed Deferred Annuities (SPRA) Includes: accounts/ contracts funded by a qualified plan rollover	RMDs apply when the account/ contract owner turns 72, 73 or 75 (depending on DOB). The first RMD can be delayed until 4/1 of the following year. If the first RMD is delayed, then take two RMDs in year 2. How to calculate RMD: Refer to Example 1 below.	SEPs & SIMPLEs: Plan sponsors and participants making/ receiving contributions to an IRA-based employer-sponsored qualified plan in the year they turn 72, 73, or 75 (depending on DOB) or after, may do so (assuming they have the earned income), however, these plans are also subject to RMDs. Note: Individual Roth IRAs and non-qualified annuity contracts do not have lifetime RMD requirements (inherited Roth IRAs and non-qualified annuities may require distributions by the beneficiary).

GROUPING FOR AGGREGATION RULE	MARKET PLAN TYPE	AVAILABLE PRODUCTS	RMD DUE DATE AND CALCULATION	NOTES AND EXCEPTIONS
GROUP 2 Employer Sponsored Defined Contribution/ Benefit Plans An RMD must be taken from each account. No aggregation permitted with any type of account, except multiple 403(b) accounts, which may be aggregated with each other.	401(k) including Designated Roth Accounts or DRACs starting in 2024. Solo or Self-Directed 401k that is not a PDIA Profit Sharing Money Purchase Cash Balance/ DB 403(b)457(b)	All products/ investment vehicles permitted by the plan.	RMDs apply when the account/ contract owner turns 72, 73, or 75 (depending on DOB). The first RMD can be delayed until 4/1 of the following year. If the first RMD is delayed, then take two RMDs in year 2. How to calculate RMD: Refer to Example 2 below.	5% or less owners and non-owner employees can delay RMDs on plan assets until the year they retire/separate from service. Can only delay RMDs from current employer plans; RMDs are still due for previous employer plans (and RMD liabilities on these previous employer plans cannot be aggregated unless/until they have been properly rolled to an IRA). While Group 2 account types can generally be rolled over to an IRA, RMDs (if applicable) must be taken first.

GROUPING FOR AGGREGATION RULE	MARKET PLAN TYPE	AVAILABLE PRODUCTS	RMD DUE DATE AND CALCULATION	NOTES AND EXCEPTIONS
GROUP 3 Annuitized Income by buying immediate annuity or annuitizing existing annuity Each annuity contract must cover its own RMD liability. No aggregation with any type of account, with one exception (see last column*)	Traditional IRA Solo or Self-Directed 401(k) that is a PDIA	Variable Annuity annuitized (Fixed, Variable and Portfolio-Income Plans) Fixed Deferred Annuity annuitized (Fixed, or Portfolio Income Plans) Single Premium Immediate Annuity (SPIA) Portfolio Immediate Income Annuity (PIIA) Portfolio Deferred Income Annuities (PDIA) Qualified Longevity Annuity Contract (PDIA in the QLAC Market)	All products except QLACs: RMDs apply when the account/contract owner turns 72, 73, or 75 (depending on DOB). The first RMD can be delayed until 4/1 of the following year. If the first RMD is delayed, then take two RMDs in year 2. Income annuities are generally not designed to allow for delaying the first RMD. It is the client's responsibility to ensure that RMDs are met, based on the specifics of their situation. QLACs: Income payments from the PDIA in the QLAC IRA market must begin no later than the earlier of the Owner's or the Joint Annuitant's 85th birthday. Calculation: Income annuities that have income plans/periods certain that do not extend payments past the IRA owner's life expectancy (as determined by IRS table), are assumed to meet their own RMD requirements. Single and Joint Life annuities (with or without a period certain or refund feature) are also assumed to meet their own RMD requirements. How to calculate RMDs when you annuitize or buy an immediate annuity in an IRA or qualified plan: Refer to Examples 3-6 below.	Exception: Under Secure Act 2.0, immediate income annuities purchased in the year an IRA owner is subject to RMDs or after, and deferred annuities that are annuitized (i.e., income is started in the year someone is subject to RMDs or after), income payments from the annuity can be used to meet an IRA owner's overall IRA RMD liability for the year of purchase or future years. Example 3 below is a common illustration of when this exception may apply. More complicated situations are discussed in Examples 4, 5 and 6. **The safe thing to do in all scenarios is to first take an RMD and then buy the immediate annuity or annuitize the annuity contract to make sure the full RMD for the year is taken rather than rely on the annuity payments meeting some or all of the RMD for the year.**

Examples

1. On December 31, 2022, a 73-year-old married individual has these account balances: $100,000 in a Traditional IRA, $100,000 in a SIMPLE IRA, and $100,000 in an Inherited IRA that she inherited from her deceased mother in 2020. To calculate her 2023 RMDs, she can aggregate the traditional and SIMPLE IRAs and take some of her RMD from both or all of it from either. For the inherited IRA, she must calculate her RMD separately using the Single Life table and take an RMD from it. For her traditional and SIMPLE IRA she uses the Uniform Life Table, which requires a 73-year-old to use a withdrawal factor of 26.5, which means she divides her previous year end account balance by 26.5. Thus, she must take $7,547 from her Traditional and SIMPLE IRAs ($200,000/26.5) and $6,098 from her inherited IRA ($100,000/16.4).

2. Same facts as in Example 1, except the 73-year-old also has two separate 401(k) accounts from different former employers. Each account has $150,000 value on December 31, 2022 and she would like to calculate her RMDs for all of her accounts for 2023. The good news is nothing changes for the IRAs above since they cannot be combined with qualified plans to determine RMDs. Since the 401(k) accounts are from different employers, she must calculate and take an RMD for each one as follows: $150,000/26.5=$5,660 RMD must be taken from each 401(k). Note that if, in 2023, she wanted to roll one of her 401(k) accounts to her Traditional IRA, she would have to take the full RMD of $5,660 from the 401(k) prior to the IRA rollover since her 2023 RMD is based on her previous year December 31, 2022 account balance.

3. A 73-year-old individual has $1,000,000 in a traditional IRA on December 31, 2022. Per the IRS Uniform Life Table, the individual has an RMD of $37,735 ($1,000,000/26.5) that must be distributed from the Traditional IRA by December 31, 2023. On July 1, 2023, he decides to purchase an immediate income annuity (SPIA Single or Joint Life, 20 years certain) with $250,000 of these IRA assets. He sets the income start date for October 1, 2023 and choses to receive payments monthly.

   In this situation, the IRA owner can elect to use the three payments received from the income annuity in 2023 (October 1, November 1, and December 1) towards their 2023 RMD (due out by December 31, 2023). If these payments from the income annuity are not enough to meet the full RMD liability, the difference will need to be taken from the non-annuitized IRA assets ($750k, assuming no market movement). To play it safe, he could take the full RMD for the year and then buy the annuity.

4. A 73-year-old individual has $1,000,000 in a traditional IRA on December 31, 2022. Per the IRS Uniform Life Table, she has an RMD of $37,735 ($1,000,000/26.5). On July 1 of 2023, she decides to purchase an immediate income annuity (Single or Joint Life, 20 years certain) with $250,000 of these IRA assets. She sets the income start date for July 1, 2024 (NM SPIAs and PIIAs allow for an income start date to be up to 13 months from contract issue) and would like to receive payments monthly.

   Because the assets allocated to the immediate income annuity were part of the December 31, 2022 IRA account value (which was used to determine the 2023 RMD liability), but the income start date for the annuity isn't until 2024, the non-annuitized IRA assets will need to be tapped to meet the entire IRA RMD liability due by December 31, 2023.

   For 2024 IRA RMD liabilities, Northwestern Mutual will provide a December 31, 2023 value for the immediate income annuity. This must be added to the December 31, 2023 value of the non-annuitized IRA, to determine the individual's RMD liability for 2024 (due by December 31, 2024).

5. A 73-year-old individual has $250,000 in a Traditional IRA as of December 31, 2022. Per the IRS Uniform Life Table, he has an RMD of $9,434 ($250,000/26.5) that must be distributed from the traditional IRA by December 31, 2023. On January 1, 2023, he decides to purchase an immediate income annuity with the entire $250,000, but he does not want the income to begin until January 1, 2024. In order to meet RMD requirements, he must be sure to take the RMD due for 2023 before purchasing the immediate income annuity. This means the IRA owner will not be able to put the full $250,000 into the immediate income annuity.

6. A 60-year-old single individual has $1,000,000 in a traditional IRA (as of 2023). He has no current RMD requirements and decides to purchase a PDIA with $250,000 of those IRA assets. He wants income from the PDIA to begin in the year he turns 73 (2036). He will be reinvesting dividends to income additions until income starts. To ensure compliance with RMD requirements on the PDIA, Northwestern Mutual will restrict the maximum deferral/income start date on the PDIA, such that a full year of payments are made the year he turns 73). For example, if he would like to take monthly payments, Northwestern Mutual will require an income start date of January 31 or earlier to ensure that all 12 annuity payments are out by December 31 of the year he is required to start taking RMDs. If he wanted to defer the first payment on the PDIA as long as possible, then he would need to select annual payments, and the income start date could then be set to December 31 of the year RMDs start. However, note, that payment frequency cannot be changed once income starts, so he will receive the annuity payments annually for life.

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