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SECURE Act Proposed Regulations

Some answers, more questions

The SECURE Act passed in late 2019, changing numerous retirement plan rules. In late February 2022, the Treasury Department finally issued proposed regulations to fill out and implement the SECURE Act. While the proposed regulations give us answers to some questions, they are merely proposals, and final regulations will likely differ after comments are received from the public.

What is a proposed regulation?

The IRS issues regulations with the approval of the Secretary of Treasury and represent the executive branch's official interpretation of a statute. Generally, final regulations have the force and effect of law to the extent they are not inconsistent with the statute. A regulation is first proposed when published in the *Federal Register* and in the *Internal Revenue Bulletin*. Proposed regulations provide guidance concerning Treasury's interpretation of a Code section. The public is given an opportunity to comment on a proposed regulation and a public hearing may be held when enough requests to speak at a public hearing are received.

Proposed regulations do not have the force of law, except that proposed regulations can be cited as substantial authority for avoiding the underpayment of income tax liability under Section 6662(b)(2).

Key Points

Post-death retirement plan distributions

- <u>Multiple beneficiaries</u>. If the account lists multiple individual designated beneficiaries and at least one of those designated beneficiaries is NOT an eligible designated beneficiary, the account is treated as not having an eligible designated beneficiary, meaning the 10-year rule applies for all designated beneficiaries. However, there are exceptions, including (1) if the eligible designated beneficiary is a minor child of the account owner, then the account is treated as having an eligible designated beneficiary even if the other designated beneficiaries are not eligible designated beneficiaries; (2) multi-beneficiary trusts; and (3) if the IRA or qualified plan is divided into separate accounts for each beneficiary. Prop. Treas. Reg. § 1.409(a)(9)-4(e)(2).

- <u>Age of majority</u>. If a plan participant or IRA owner dies, and that owner's minor child is a beneficiary of the retirement account, that minor child of the account owner is an eligible designated beneficiary not subject to the 10-year rule until the minor child reaches the age of majority. The proposed regulations state that an individual reaches the age of majority on that individual's 21st birthday. Prop. Treas. Reg. § 1.409(a)(9)-4(e)(3).

Comment: When SECURE act passed, some commentators believed the age of majority under state law would apply. Using the minor child's 21st birthday simplifies things since there would not be different dates depending upon state law.

- 10-year rule for defined contribution plans. The SECURE Act requires that inherited defined contribution qualified accounts be completely distributed to a designated beneficiary within 10 years of the account owner's death.

  - *Death Before Required Beginning Date*: The proposed regulations extend the deadline for distribution of the account balance to the end of the 10th calendar year following death. There is no requirement for annual distributions, merely that the entire account balance be distributed by the end of the 10th year following death. Prop. Treas. Reg. § 1.401(a)(9)-3(c).

  - *Death After Required Beginning Date*: The proposed rule would require an annual RMD based on the designated beneficiary's life expectancy, and a lump sum of the entire remaining balance must be distributed by the end of the 10th year following the account owner's death. Prop. Treas. Reg. §§ 1.401(a)(9)-2(a)(4), 1.401(a)(9)-5(e).

    Comment: The SECURE Act states that except in the case of a beneficiary who is not a designated beneficiary, the 5-year rule shall apply except that 10 years is used instead of 5. The 5-year rule has been in the regulations since 1985 and has never been interpreted as requiring annual RMDs. The proposal to require annual RMDs in addition to the SECURE Act requirement of the account being completely distributed by the end of the 10th year is a potentially momentous change, and one which seems likely to generate significant pushback during the public comment period.

- Disabled or chronically ill beneficiary. For purposes of determining whether a beneficiary is disabled or chronically ill, documentation of the disability or chronic illness would have to be provided to the plan administrator no later than October 31 of the year following the plan participant's death. "Disabled" and "chronically ill" are defined. Prop. Treas. Reg. §§ 1.409(a)(9)-4(e)(4) & (5).

  Comment: There is not a clear understanding of what this means for IRA custodians since IRA custodians are not required to determine or report disability. This provision will likely generation numerous comments.

- Spouse as sole beneficiary. If an account owner dies before his RBD and his spouse is the sole beneficiary, the surviving spouse can defer RMDs until the account owner's RBD (when the deceased spouse would have turned 72). Prop. Treas. Reg. § 1.401(a)(9)-3(d).

- Spousal rollover timeframe. If the account owner's surviving spouse is the designated beneficiary, and the surviving spouse wants to do a spousal rollover, the spousal rollover election must be made by the later of (1) the end of the calendar year in which the surviving spouse turns 72; or (2) the end of the calendar year following the year of the account owner's death. Prop. Treas. Reg. § 1.408-8(c).

Comment: This would be a change from the existing rule which allows a surviving spouse to do a spousal rollover at any time.

Qualified Longevity Annuity Contracts (QLACs)

The proposed regulations would allow a QLAC to provide a cash surrender value prior to the employee's RBD. Prop. Treas. Reg. § 1.401(a)(9)-6(q).

Applicability Date

The regulations are proposed to apply for purposes of determining RMDs for calendar years beginning on or after January 1, 2022. For calendar year 2021 distributions, taxpayers must use existing regulations but reflect a "good faith" interpretation of the SECURE Act. The proposed regulations do not extend the good faith relief to RMDs due in 2022.

Comments and Public Hearing

Comments are due 90 days after the proposed regulations are published in the Federal Register. A public hearing is scheduled for June 15, 2022.

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