Five Ways SECURE 2.0 Changes the Required Minimum Distribution Rules

The RMD rules are designed to spread out the distribution of your entire interest in an IRA or plan account over your lifetime. The purpose of the RMD rules is to ensure that funds are utilized during retirement, instead of remaining untouched and benefiting from continued tax-deferral until left as an inheritance. RMDs generally have the effect of producing taxable income during your lifetime.

The SECURE 2.0 legislation included in the $1.7 trillion appropriations bill passed late last year builds on changes established by the original Setting Every Community Up for Retirement Enhancement Act (SECURE 1.0) enacted in 2019. SECURE 2.0 includes significant changes to the rules that apply to required minimum distributions from IRAs and employer retirement plans. Here's what you need to know.

What Are Required Minimum Distributions (RMDs)?

Required minimum distributions, sometimes referred to as RMDs or minimum required distributions, are amounts that the federal government requires you to withdraw annually from traditional IRAs and employer retirement plans after you reach a certain age, or in some cases, retire. You can withdraw more than the minimum amount from your IRA or plan in any year, but if you withdraw less than the required minimum, you will be subject to a federal tax penalty.

These lifetime distribution rules apply to traditional IRAs, Simplified Employee Pension (SEP) IRAs and Savings Incentive Match Plan for Employees (SIMPLE) IRAs, as well as qualified pension plans, qualified stock bonus plans, and qualified profit-sharing plans, including 401(k) plans. Section 457(b) plans and Section 403(b) plans are also generally subject to these rules. (If you are uncertain whether the RMD rules apply to your employer plan, you should consult your plan administrator or a tax professional.)

Here is a brief overview of the top five ways that the new legislation changes the RMD rules.

1. Applicable Age for RMDs Increased

Prior to passage of the SECURE 1.0 legislation in 2019, RMDs were generally required to start after reaching age 70½. The 2019 legislation changed the required starting age to 72 for those who had not yet reached age 70½ before January 1, 2020.

SECURE 2.0 raises the trigger age for required minimum distributions to age 73 for those who reach age 72 after 2022. It increases the age again, to age 75, starting in 2033. So, here's when you have to start taking RMDs based on your date of birth:

Date of Birth	Age at Which RMDs Must Commence
Before July 1, 1949	70½
July 1, 1949, through 1950	72
1951 to 1959	73
1960 or later[1]	75

Your first required minimum distribution is for the year that you reach the age specified in the chart, and generally must be taken by April 1 of the year following the year that you reached that age. Subsequent required distributions must be taken by the end of each calendar year (so if you wait until April 1 of the year after you attain your required beginning age, you'll have to take two required distributions during that calendar year). If you continue working past your required beginning age, you may be able to delay RMDs from your current employer's retirement plan until after you retire.

2. RMD Penalty Tax Decreased

The penalty for failing to take a required minimum distribution is steep — historically, a 50% excise tax on the amount by which you fell short of the required distribution amount.

SECURE 2.0 reduces the RMD tax penalty to 25% of the shortfall, effective this year (still steep, but better than 50%).

Also effective this year, the Act establishes a two-year period to correct a failure to take a timely RMD distribution, with a resulting reduction in the tax penalty to 10%. Basically, if you self-correct the error by withdrawing the required funds and filing a return reflecting the tax during that two-year period, you can qualify for the lower penalty tax rate.

3. Lifetime Required Minimum Distributions from Roth Employer Accounts Eliminated

Roth IRAs have never been subject to lifetime Required Minimum Distributions. That is, a Roth IRA owner does not have to take RMDs from the Roth IRA while he or she is alive. (Distributions to beneficiaries are required after the Roth IRA owner's death, however.)

The same has not been true for Roth employer plan accounts, including Roth 401(k) and Roth 403(b) accounts. Plan participants have been required to take minimum distributions from these accounts upon reaching their RMD age or avoid the requirement by rolling over the funds in the Roth employer plan account to a Roth IRA.

Beginning in 2024, the SECURE 2.0 legislation eliminates the lifetime RMD requirements for all Roth employer plan account participants, even those participants who had already commenced lifetime RMDs. (Any lifetime RMD from a Roth employer account attributable to 2023, but payable in 2024, is still required.)

4. Additional Option for Spouse Beneficiaries of Employer Plans

The SECURE 2.0 legislation provides that, beginning in 2024, when a participant has designated his or her spouse as the sole beneficiary of an employer plan, a special option is available if the participant dies before required minimum distributions have commenced.

This provision will permit a surviving spouse to elect to be treated as the employee, similar to the already existing provision that allows a surviving spouse who is the sole designated beneficiary of an inherited IRA to elect to be treated as the IRA owner. This will generally allow a surviving spouse the option to delay the start of required minimum distributions until the deceased employee would have reached the appropriate RMD age, or until the surviving spouse reaches the appropriate RMD age, whichever is more beneficial. This will also generally allow the surviving spouse to utilize a more favorable RMD life expectancy table to calculate distribution amounts.

5. New Flexibility Regarding Annuity Options

Starting in 2023, the SECURE 2.0 legislation makes specific changes to the required minimum distribution rules that allow for some additional flexibility for annuities held within qualified employer retirement plans and IRAs. Allowable options may include:

- Annuity payments that increase by a constant percentage, provided certain requirements are met
- Lump-sum payment options that shorten the annuity payment period
- Acceleration of annuity payments payable over the ensuing 12 months
- Payments in the nature of dividends
- A final payment upon death that does not exceed premiums paid less total distributions made

These are just a few of the many provisions in the SECURE 2.0 legislation. The rules regarding required minimum distributions are complicated. While the changes described here provide significant benefit to individuals, the rules remain difficult to navigate, and you should consult a tax professional to discuss your individual situation.

It is important to understand that purchasing an annuity in an IRA or an employer-sponsored retirement plan provides no additional tax benefits beyond those available through the tax-deferred retirement plan. Qualified annuities are typically purchased with pre-tax money, so withdrawals are fully taxable as ordinary income, and withdrawals prior to age 59½ may be subject to a 10% federal tax penalty.

1 A technical correction is needed to clarify the transition from age 73 to age 75 for purposes of the required minimum distribution rule. As currently written, it is unclear what the correct starting age is for an individual born in 1959 who reaches age 73 in the year 2032.

Borrowing or Withdrawing Money from Your Retirement Plan

If you have a retirement plan at work and need some cash, you might be tempted to borrow or withdraw money from it. But keep in mind that the purpose of a retirement plan is to save for retirement. Take money out of it now, and you'll risk running out of money during retirement. You may also face stiff tax consequences and penalties for withdrawing money before age 59½. Still, if you're facing a financial emergency — for instance, your child's college tuition is almost due and your retirement plan is your only source of available funds — borrowing or withdrawing money from your retirement plan may be your only option.

Plan loans

To find out if you're allowed to borrow from your retirement plan and under what circumstances, check with your plan's administrator or read your summary plan description. This can be found under Forms & Reports & Info online.

Generally, obtaining a retirement plan loan is relatively easy — there's little paperwork, and there's no credit check.

How much can you borrow?

No matter how much you have in your retirement plan, you probably won't be able to borrow the entire sum. Generally, you can't borrow more than $50,000 or one-half of your vested plan benefits, whichever is less. Your plan may also allow you to borrow up to $100,000 (or 100% of your vested plan benefits, whichever is less) if used for recovery from a federally-declared disaster.

What are the requirements for repaying the loan?

Typically, you have to repay money you've borrowed from your retirement plan within five years by making regular payments of principal and interest through payroll deduction. However, if you use the funds to purchase a primary residence, you may have a much longer period of time to repay the loan. Refer to your Summary Plan Description for your plan's loan policy.

Make sure you follow to the letter the repayment requirements for your loan. If you don't repay the loan as required, the money you borrowed will be considered a taxable distribution. If you're under age 59½, you'll owe a 10% federal penalty tax, as well as regular income tax, on the outstanding loan balance (other than the portion that represents any after-tax or Roth contributions you've made to the plan).

What are the advantages of borrowing money from your Retirement Plan?

- You won't pay taxes and penalties on the amount you borrow, as long as the loan is repaid on time
- Interest rates on retirement plan loans must be consistent with the rates charged by banks and other commercial

institutions for similar loans
- The interest you pay on borrowed funds is credited to your own plan account; you pay interest to yourself, not to a bank or other lender

What are the disadvantages of borrowing money from your Retirement Plan?

- If you don't repay your plan loan when required, it will generally be treated as a taxable distribution.
- If you leave your employer's service (whether voluntarily or not) and still have an outstanding balance on a plan loan, the outstanding amount of the loan will be considered a distribution. You'll usually be required to repay the amount in full [or roll over the amount to another retirement plan or IRA] by the tax filing deadline (including extensions) of the year following the year the amount is determined to be a distribution (i.e., the year you leave your employer). Otherwise, the outstanding balance will be treated as a taxable distribution, and you'll owe a 10% penalty tax (if you're under age 59½) in addition to regular income taxes.
- Loan interest is generally not tax deductible (unless the loan is secured by your principal residence).
- The amount you borrow is removed from your retirement plan account, and your loan payments are credited back to your account. You'll lose out on any tax-deferred (or, in the case of Roth accounts, potentially tax-free) investment earnings that may have accrued on the borrowed funds had they remained in your retirement pllan account.
- Loan payments are made with after-tax dollars.

Hardship withdrawals

Your retirement plan may have a provision that allows you to withdraw money from the plan while you're still employed if you can demonstrate "heavy and immediate" financial need, have exhausted all other available distribution options from your retirement plans, and have no other resources you can use to meet that need (e.g., you can't borrow from a commercial lender and you have no other available savings). It's up to your employer to determine which financial needs qualify. Many employers allow hardship withdrawals only for the following reasons:

- To pay the medical expenses of you, your spouse, your children, your other dependents, or your primary beneficiary
- To pay the burial or funeral expenses of your parent, your spouse, your children, your other dependents, or your primary beneficiary
- To pay a maximum of 12 months worth of tuition and related educational expenses for post-secondary education for you, your spouse, your children, your other dependents, or your plan beneficiary
- To pay costs related to the purchase of your principal residence
- To make payments to prevent eviction from or foreclosure on your principal residence
- To pay expenses for the repair of damage to your principal residence after certain casualty losses
- To pay expenses and losses (including loss of income) incurred as a result of a disaster declared by the Federal Emergency Management Agency, such as a hurricane or wildfire (provided the participant's principal residence or place of employment is located in the federally declared disaster area)[1]

Note: You may also be allowed to withdraw funds to pay income tax and/or penalties on the hardship withdrawal itself, if these are due.

Your employer may require that you certify your need for a hardship withdrawal in writing, and certify that you have experienced a heavy and immediate financial need.

How much can you withdraw?

Depending on plan rules, you may be able to withdraw your contributions, safe harbor employer contributions, and your employer's qualified nonelective and matching contributions, as well as earnings on those contributions. Check with your plan administrator or Summary Plan Description for more information on the rules that apply to withdrawals from your retirement plan.

What are the advantages of withdrawing money from your Retirement Plan in cases of hardship?

The option to take a hardship withdrawal can come in very handy if you really need money and you have no other assets to draw on, and your plan does not allow loans (or if you can't afford to make loan payments).

What are the disadvantages of withdrawing money from your Retirement Plan in cases of hardship?

- Taking a hardship withdrawal will reduce the size of your retirement nest egg, and the funds you withdraw will no longer grow tax deferred.
- Hardship withdrawals are generally subject to federal (and possibly state) income tax. A 10% federal penalty tax may also apply if you're under age 59½. [If you make a hardship withdrawal of your Roth contributions, only the portion of the withdrawal representing earnings will be subject to tax and penalties.][1-2]

What else do I need to know?

If you are a reservist called to active duty after September 11, 2001, special rules may apply to you.

[1] Your employer may offer penalty-free qualified disaster recovery distributions (QDRDs) to retirement plan participants affected by federally-declared disasters, up to a maximum of $22,000 per disaster.

[2] The entire 401(k) plan balance may be eligible for penalty-free distributions.

Exceptions to the 10% Early-Withdrawal Penalty

Withdrawing taxable funds from a tax-deferred retirement account before age 59½ generally triggers a 10% federal income tax penalty, on top of any federal income taxes due. [Distributions from Section 457(b) plans are generally not subject to an early distribution penalty; and the penalty for distributions from SIMPLE IRA plans during your first two years of participation is 25%, 10% thereafter.] However, there are certain situations in which you are allowed to make early withdrawals from a retirement account and avoid the tax penalty. (Check your specific plan provisions to see whether a particular withdrawal option is available.)

IRAs and employer-sponsored retirement plans have different exceptions, although the rules are similar.

IRA exceptions

The following distributions are not subject to the 10% penalty tax:

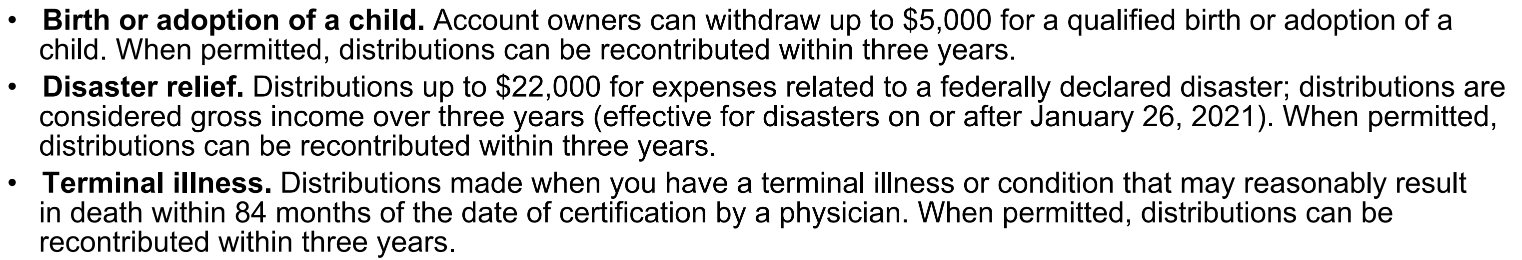
- **Death of the IRA owner.** Distributions to your designated beneficiaries after your death. Most non-spouse beneficiaries must liquidate the inherited accounts within 10 years.
- **Disability.** Distributions made due to your qualifying disability.
- **Unreimbursed medical expenses.** Distributions equal to the amount of your unreimbursed medical expenses that exceed 7.5% of your adjusted gross income in a calendar year. (You don't have to itemize deductions to use this exception, and the distributions don't have to actually be used to pay those medical expenses.)
- **Medical insurance.** Distributions made to pay for health insurance if you've lost your job and are receiving unemployment benefits.
- **Substantially equal periodic payments (SEPPs).** Distributions you receive as a series of substantially equal payments over your life expectancy, or the combined life expectancies of you and your beneficiary. You must withdraw funds at least annually based on one of three rather complicated IRS-approved distribution methods. You generally can't change or alter the payments for five years or until you reach age 59½, whichever occurs later. If you do you'll again wind up having to pay the 10% penalty tax on the taxable portion of all your pre-59½ SEPP distributions (unless another exception applies).
- **Qualified higher-education expenses** for you and/or your dependents.
- **First home purchase,** up to $10,000 (lifetime limit).
- **Qualified reservist distributions.** Certain distributions to qualified military reservists called to active duty.
- **Birth or adoption of a child.** Account owners can withdraw up to $5,000 for a qualified birth or adoption of a child. When permitted, distributions can be recontributed within three years.
- **Disaster relief.** Distributions up to $22,000 for expenses related to a federally declared disaster; distributions are considered gross income over three years (effective for disasters on or after January 26, 2021). When permitted, distributions can be recontributed within three years.
- **Terminal illness.** Distributions made when you have a terminal illness or condition that may reasonably result in death within 84 months of the date of certification by a physician. When permitted, distributions can be recontributed within three years.

Employer-sponsored plan exceptions

Note: Some of the distribution types listed below are optional in retirement plans. Check with your plan administrator, or your Summary Plan Description for more information.

The following distributions are not subject to the 10% penalty tax:

- **Death of the plan participant.** Upon your death, your designated beneficiaries may begin taking distributions from your account. Most non-spouse beneficiaries must liquidate the inherited accounts within 10 years.
- **Disability.** Distributions made due to your qualifying disability.
- **Part of a SEPP program** (see above). Distributions you receive as a series of substantially equal payments over your life expectancy, or the combined life expectancies of you and your beneficiary. You generally cannot modify the payments for a period of five years or until you reach age 59½, whichever is longer.
- **Attainment of age 55.** Distributions made to you upon separation of service from your employer. The separation must have occurred during or after the calendar year in which you reached the age of 55 (age 50 for qualified public safety employees).
- **Qualified Domestic Relations Order (QDRO).** Payments made to an alternate payee under a QDRO.
- **Medical care** (see above). Distributions equal to the amount of your unreimbursed medical expenses that exceed 7.5% of your adjusted gross income in a calendar year.
- **To reduce excess contributions/deferrals.** Distributions made to correct excess contributions you or your employer made to the plan over the allowable limits.
- **Qualified reservist distributions.** Certain distributions to qualified military reservists called to active duty.



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- **Terminal illness.** Distributions made when you have a terminal illness or condition that may reasonably result in death within 84 months of the date of certification by a physician. When permitted, distributions can be recontributed within three years.

If you plan to withdraw funds from a tax-deferred account, make sure to carefully examine the rules on exemptions for early withdrawals. For more information on situations that are exempt from the early-withdrawal income tax penalty, visit the IRS website at www.irs.gov.

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