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**Steve Leimberg's Employee Benefits and Retirement Planning Email Newsletter - Archive Message #776**

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| **Date:** | **21-Jan-22** |
| **From:** | **Steve Leimberg's Employee Benefits and Retirement Planning Newsletter** |
| **Subject:** | **Vanessa L. Kanaga and Natalie B. Choate: New Life Expectancy Tables - An Opportunity to Provide Value to Clients** |

*"New IRS life expectancy tables are in effect for calculating clients' RMDs in 2022 and later years. This month, the IRS completed the picture by also updating the 'life expectancy' tables used for calculating 'SOSEPPs' (series of substantially equal periodic payments), a popular method of avoiding the 10% tax on pre-age-59½ distributions. Advisors can add value for clients by understanding how to use these tables."*

We close the week with important and timely commentary by **Vanessa Kanaga** and **Natalie Choate** on the new life expectancy tables. Members who wish to learn more about this topic should consider joining **Bob Keebler** in his exclusive **LISI** Webinar titled: "IRS Notice 2022-06 Is a Game Changer for Clients Retiring Before 59 1/2, Everything Just Changed for IRAs" on Tuesday, January 25th. Click this link to learn more: Bob Keebler

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**Natalie B. Choate** is a lawyer in Wellesley, Massachusetts. Her practice is limited to consultations with other estate planning lawyers on matters of estate planning, and trust and estate administration, for retirement benefits. She is the author of the advisor's "bible" on estate and distribution planning for IRAs and other retirement plans, Life and Death Planning for Retirement Benefits (8th ed. 2019). The book is available in printed form at www.ataxplan.com, or in an electronic edition via subscription at www.retirementbenefitsplanning.us. Though the book has not been updated for SECURE, a summary and analysis of SECURE's changes is posted free at www.ataxplan.com.

Here is their commentary:

## COMMENT:

New IRS life expectancy tables are in effect for calculating clients' RMDs in 2022 and later years. This month, the IRS completed the picture by also updating the "life expectancy" tables used for calculating "SOSEPPs" (series of substantially equal periodic payments), a popular method of avoiding the 10% tax on pre-age-59½ distributions. Advisors can add value for clients by understanding how to use these tables.

It is not news that retirement benefits, including Individual Retirement Accounts (IRAs) and qualified plans such as 401(k) plans, have become a central component of estate planning in recent years, as the value of these accounts has grown for many Americans.  Most estate planning professionals advise clients on planning strategies for these assets, including strategies for minimizing income tax on required minimum distributions (RMDs) from these plans and IRAs during life and after death.  However, many planners do not often delve into the gritty details of how those RMDs are calculated, for good reason.  The advisor is focused on the high-level structure of the plan, not the administrative details which are in the hands of the plan administrator or IRA custodian.

2022 offers estate planners an opportunity to provide value to their clients by digging a little deeper into these administrative details.  As of January 1, 2022, new life expectancy and applicable distribution period tables went into effect with respect to the determination of RMDs.  These new tables extend the life expectancy used in calculating RMDs for most individuals taking distributions during life, and for most beneficiaries of IRAs and qualified plans after the participant's death.  These adjusted tables have the potential to result in lower RMDs for many retirees and their beneficiaries, but only if distributions are correctly calculated taking into account the new life expectancy figures.  Given that it has been two decades since the IRS last modified the life expectancy tables, it is easy to imagine that some RMDs may be calculated incorrectly while everyone adjusts to this change.

Advisors can be of service to their clients by alerting them to this change and helping to ensure their RMDs are calculated correctly. Fortunately, the rules for using the tables are relatively easy to understand and apply. Discussed below are the rules for applying three updated life expectancy tables: The Uniform Lifetime Table and the Single Life Table, both located in Treas. Reg. § 1.401(a)(9)-9, and the Uniform Lifetime Table~~,~~ as applied to individuals younger than age 72 (the age used in defining the "required beginning date" under I.R.C. § 401(a)(9)), located in IRS Notice 2022-6.

These tables are discussed in the context of the individual to whom they apply. Each of the following sections is organized by a header that is meant to complete the sentence, "My client is... ."

<u>Past the Required Beginning Date, Taking Lifetime Distributions</u>

Individuals who have hit the required beginning date[i] and are taking lifetime distributions use the Uniform Lifetime Table to calculate RMDs (unless the sole beneficiary of the plan is the participant's more than 10 years younger spouse[ii]). The advantage of the Uniform Lifetime Table is that the distribution periods set forth in the table are based on the joint and survivor life expectancy of a participant and a hypothetical beneficiary who is 10 years younger than the participant, providing for a longer distribution period. Another advantage afforded for lifetime RMDs is that they are recalculated each year, by returning to the Uniform Lifetime Table to determine the distribution period based on the participant's age in that year.[iii] This makes it easy to apply the new Uniform Lifetime Table to a client taking lifetime RMDs: Simply determine the age of the client as of the client's birthday in that year, find the corresponding distribution period divisor in the table, and divide the account balance as of December 31 of the prior year by that divisor.

For example: Jan, who has been taking RMDs from an IRA for several years, is turning 80 this year, so the distribution period per the Uniform Lifetime Table is 20.2. The IRA account balance as of December 31, 2021, was $2 million. Jan's RMD for 2022 is $99,009.90 ($2 million/20.2).

The new Uniform Lifetime Table is effective for determining RMDs as of January 1, 2022.

Taking Lifetime Distributions Under the SOSEPP Exception, Using the RMD Method

Generally, plan participants and IRA owners are subject to a 10% penalty on distributions taken prior to attaining age 59.5.[iv] One method of avoiding the 10% penalty on pre-age 59.5 distributions is to take a "series of substantially equal periodic payments" (SOSEPP). The IRS has provided elaborate rules about how to set these up. One way of computing the payments is the "RMD method" whereby payments are computed using the prior year end account balance divided by a factor from the RMD tables---you can use the Single Life Table, the Joint and Last Survivor Table or the Uniform Lifetime Table (all found in Treas. Reg. § 1.401(a)(9)-9). Whichever of those three tables is selected when the RMD method is chosen must continue to be used for the rest of the duration of the SOSEPP; you cannot, for example, switch from the Single Life Table to the Uniform Lifetime Table once you have started your SOSEPP. Like RMDs calculated using the Uniform Lifetime Table following the required beginning date, SOSEPP distributions using the RMD method are recalculated annually based on the participant's age as of the participant's birthdate in that year. Rev. Rul. 2002-62 created this "RMD method" and also provided a "Uniform Lifetime Table" for younger ages since the real Uniform Lifetime Table didn't start until age 70.5 (the "required beginning date age" prior to 2020).

Anyone taking distributions under a SOSEPP can switch to the RMD method any time even if the SOSEPP was originally set up using a different method. However, what one cannot do is “modify” the SOSEPP distributions before the participant reaches age 59.5 (or for at least 5 years after starting the SOSEPP). Such a modification would disqualify the entire SOSEPP, resulting in application of the 10% penalty plus interest on all payments received.[v] The one-time switch to the “RMD method” from one of the other methods of constructing a SOSEPP is not deemed a “modification” for this purpose.

As of January 1, 2022, the IRS had stated that it anticipated issuing guidance to update Rev. Rul. 2002-62 in light of the new life expectancy tables, but had not yet done so. Fortunately, on January 18 of this year, the IRS issued Notice 2022-6, which supersedes and replaces Rev. Rul. 2002-62. In addition to providing other guidance regarding the use of SOSEPPS and the various calculation methods available, the Notice sets forth a new Uniform Lifetime Table for individuals under age 72 (the age at which the real Uniform Lifetime Table now starts).

Notice 2022-6 states that it replaces Rev. Rul. 2002-62 for any series of payments commencing on or after January 1, 2023, and that it "may be used for a series of payments commencing in 2022." Importantly, it also states that for SOSEPP distributions beginning prior to 2023 using the RMD method, the new Single Life Table or Joint and Last Survivor Table provided in the Regulations, or the Uniform Lifetime Table for younger ages, provided in the Notice, may be used for payments in the series without the use of the new tables being considered a modification that would subject the payment to penalty as described above.

This means that an individual taking distributions under an RMD SOSEPP that commenced prior to 2022 may continue to use the old tables, i.e., the tables that were used when the RMD-method SOSEPP began. Certain other aspects of this transition rule are unclear, such as: whether a switch to the new tables must be made in 2022-2023 or could be made in any later year; and whether a person whose SOSEPP started prior to 2022 but then switches to the RMD method after 2022, has the option, upon making that switch, to use either set of tables. Further IRS clarification will be needed for these and similar fine points.

Whether the client would prefer to use the "old" numbers or the "new" numbers may depend on the client's age and financial position.

For example: Steve, who will turn 45 in 2022, has been taking distributions from his qualified plan under a SOSEPP since 2019. His SOSEPP uses the “RMD method” with the Uniform Lifetime Table. His account balance, as of December 31, 2021, is $1 million. Under the new Uniform Lifetime Table for younger ages, published in Notice 2022-6, the life expectancy divisor for 2022 would be 53.4, so his distribution for 2022 would be $18,726.59. Under the "old" tables, his 2022 distribution would have been $19,417.48. If Steve is in a transitional phase of his life and needs access to additional finances, he may prefer to use the old numbers. If he has reached a point of financial stability, he may instead wish to use the new numbers in order to defer more of the income tax on his retirement assets.

<u>A Beneficiary Receiving Post-Death RMDs</u>

For beneficiaries of a qualified plan or IRA after the death of the participant, the most difficult part of the calculating the RMDs is not using the life expectancy tables, but rather determining whether the beneficiary qualifies for the life expectancy stretch at all. If the participant died on or after January 1, 2020, the date on which the SECURE Act took effect, a beneficiary of the qualified plan or IRA will not be eligible to stretch RMDs over the beneficiary's life expectancy unless the beneficiary is an "Eligible Designated Beneficiary" within the meaning of I.R.C. § 401(a)(9)(E)(ii).

This includes a relatively narrow set of designated beneficiaries: the participant's surviving spouse, a child of the participant who has not yet reached the age of majority, a chronically ill or disabled individual (within the meaning of certain statutory definitions), or an individual not previously described who is not more than 10 years younger than the participant. Although it is possible to achieve Eligible Designated Beneficiary status by creating a conduit trust for the benefit of an individual described in that list, it is important to note that (based on current regulations) an accumulation trust will not permit Eligible Designated Beneficiary status unless it qualifies as a trust for a disabled or chronically ill beneficiary described in I.R.C. § 401(a)(9)(H)(iv).

An Eligible Designated Beneficiary will be able to take RMDs over the beneficiary's life expectancy, if the plan permits such a distribution (note, however, that with respect to a minor child, the life expectancy distribution only continues until the child reaches the age of majority). A mere "designated beneficiary," including a properly drafted accumulation trust that does not fall within the exception noted above, will be required to receive all assets of the qualified plan or IRA within 10 years of the participant's death.

Now, let's assume that the client is an Eligible Designated Beneficiary, or a designated beneficiary of a plan or IRA where the participant died prior to January 1, 2020. In that case, it will be relatively easy to calculate RMDs using the updated Single Life Table in the Regulations. The method for doing so will depend on whether the participant's surviving spouse is the sole beneficiary of the plan or IRA, or whether the beneficiary is a non-spouse designated beneficiary.

*Surviving Spouse as Sole Beneficiary*

First, let's consider the situation in which the sole beneficiary is the participant's surviving spouse, which would include a conduit trust for the benefit of the surviving spouse. In that case, the RMDs are calculated using the Single Life Table, as is the case for any eligible designated beneficiary. However, a surviving spouse who is the sole beneficiary is afforded an advantage that does not apply to other beneficiaries: the surviving spouse's life expectancy is recalculated each year, based on the surviving spouse's age as of the surviving spouse's birthday in that year.

This provides a longer stretch-out period for RMDs paid to a surviving spouse as the sole beneficiary. It also makes it relatively easy to apply the new Single Life Table in calculating the RMDs to a surviving spouse. The method is essentially the same as the method for calculating RMDs during life, except the life expectancy divisor is found in the Single Life Table, rather than the Uniform Lifetime Table.

For example: Chris is the sole beneficiary of the IRA of Chris's deceased spouse, Sam, through a conduit trust that requires the trustee to pay the RMDs (as well as any other distributions the trust receives from the IRA) to Chris for Chris's life. The IRA balance as of December 31, 2021, was $3 million. Chris will turn 73 in 2022. Based on the new Single Life Table in Treas. Reg. § 1.401(a)(9)-9, Chris's life expectancy divisor in 2022 is 16.4. Accordingly, in 2022, the trustee will withdraw and distribute to Chris (after payment of applicable expenses) an RMD of $182,926.82 ($3 million/16.4).

*Non-Spouse Beneficiary*

Designated beneficiaries (pre-SECURE) and Eligible Designated Beneficiaries (post-SECURE) other than the surviving spouse also calculate RMDs using the Single Life Table published in the Regulations. However, unlike a surviving spouse who is the sole beneficiary, a non-spouse beneficiary does not re-calculate the beneficiary's life expectancy in determining RMDs each year. Instead, the beneficiary's life expectancy is determined based on the age the beneficiary will turn during the year after the year of the participant's death. In each subsequent year, the beneficiary's life expectancy is determined by subtracting one from that life expectancy. The account balance at the end of the prior year is divided by that life expectancy in order to determine the RMD.

For example, Seth designated his daughter Rachel as the beneficiary of his IRA. Seth died in 2016. In 2017, the year after Seth's death, Rachel turned 32. (Because Seth died prior to 2020 (the effective date of the SECURE Act changes), Rachel, as Seth's designated beneficiary, was and is able to use the life expectancy payout method, even though she is not in any "Eligible Designated Beneficiary" category.) Accordingly, her life expectancy, based on the Single Life Table at that time, was 51.4. That divisor was used to calculate her RMD in 2017. In 2018, her RMD was calculated using a divisor of 50.4 (the original divisor -1). In 2019, the RMD was calculated using a divisor of 49.4.

The updated life expectancy tables throw a wrinkle in this relatively simple process, because the baseline life expectancy calculations have now changed. So how does one calculate RMDs for a beneficiary whose life expectancy was established for that purpose prior to publication of the new tables? Fortunately, the Regulations provide guidance on redetermining this life expectancy calculation.[vi] Here is the process for redetermining the beneficiary's life expectancy:

1. Determining the beneficiary's life expectancy using the new Single Life Table, based on the beneficiary's age as of the beneficiary's birthday in the year following the participant's death.

2. Determine the number of years that have passed since the first year RMDs began.

3. Subtract the figure obtained in #2 from the life expectancy figure obtained in #1.

Going back to our Rachel example above: Her life expectancy divisor in the year following Seth's death (2017), using the new Single Life Table, would have been 53.4. Five years have passed since that year in which RMDs were initially paid. Accordingly, Rachel's life expectancy divisor for 2022 will be 48.4 (53.4-5). The same process applies for an Eligible Designated Beneficiary of a plan where the participant died post-SECURE but prior to 2022.[vii]

The new Single Life Table is effective for RMDs determined as of January 1, 2022.

**Conclusion**

Although life expectancy calculations may seem like an administrative detail in terms of planning for retirement benefits, an incorrect calculation can cause headaches for the client and potentially result in the client owing penalties or not getting the full advantage of the available income tax deferral. Advisors who become familiar with the updated life expectancy tables and know how to use them may be able to save their clients from the unintended consequences of a calculation error. To add a quick technical note: When searching for the new tables, be sure to find the most recent version of the Regulations (and see Notice 2022-6 for the updated Uniform Lifetime Table applicable to younger lives for those taking SOSEPPs). Subscribers to the online version of Life and Death Planning for Retirement Benefits, by Natalie B. Choate, www.retirementbenefitsplanning.us, will also find the updated tables in Appendix A of the book beginning January 25.

**HOPE THIS HELPS YOU HELP OTHERS MAKE A *POSITIVE* DIFFERENCE!**

Vanessa L. Kanaga

Natalie B. Choate

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## CITATIONS:

[i] The required beginning date differs depending on several factors, including the type of retirement account involved, whether the participant has retired, and whether the participant is a partial owner of the employer in an employer-sponsored plan. For qualified plans and traditional IRAs, the required beginning date is generally April 1 of the calendar year following the calendar year in which the individual reaches age 72, unless the participant in a qualified plan has not yet retired (and is not a "5-percent owner" as defined in I.R.C. § 416) in which case it is April 1 of the calendar year following the calendar year in which the individual retires. See I.R.C. § 401(a)(9)(C) and Treas. Reg. § 1.408-8, A-3.

[ii] In the case of a participant with a more-than-10-years younger spouse who is the sole beneficiary, RMDs will be calculated using the Joint and Last Survivor Table, located in Treas. Reg. § 1.401(a)(9)-9(d).

[iii] Treas. Reg. § 1.401(a)(9)-5, A-4(a).

[iv] I.R.C. § 72(t).

[v] I.R.C. § 72(t)(4).

[vi] Treas. Reg. 1.401(a)(9)-9(f)(2).

[vii] Also note that the same process applies even though the RMD was suspended in 2020 due to the CARES Act. RMDs in subsequent years are calculated as if the 2020 distribution had not been suspended (meaning 2020 is counted in the number of years lapsed when determining the beneficiary's life expectancy).