THE NEW IMPROVED RULES FOR MINIMUM PLAN DISTRIBUTIONS

By Clark M. Blackman II and Ellen J. Boling

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In January 2001, the government released substantial revisions to the "proposed" regulations concerning minimum distributions that will affect everyone who holds retirement assets.

The original proposed regulations were issued in 1987, and although they were never finalized, they have provided the only guidance available on the IRS's position regarding minimum distributions and beneficiary designations.

The good news is that the new 2001 proposed regulations make major simplifications to the 1987 rules, including the calculation of "required minimum distributions" during your lifetime, and the determination of a designated beneficiary for distributions after your death. As a result, the new rules make it much easier for you to understand and apply the minimum distribution and beneficiary designation rules.

If you hold retirement assets, it is important for you to understand the federal regulations regarding required retirement plan distributions so that you may determine the method of distribution most advantageous to your particular situation.

This article is the first of two that outline the primary framework and operation of the new proposed regulations. Part 1 focuses on the changes to lifetime distributions, while Part 2 outlines the impact on post-death distributions.

NEW RULES: AN OVERVIEW

In general, the need to make decisions at age 70½, which under the 1987 proposed regulations would bind the owner of the retirement assets for life (during which financial circumstances could change significantly), was perceived as unreasonably restrictive. In addition, the determination of life expectancy and designating a beneficiary, and the resulting required minimum distribution calculation, were viewed as too complex.

In response to these concerns, new proposed regulations were issued on January 11, 2001. These regulations simplify the rules:

- The regulations provide a simple, uniform table that you can use to determine your required minimum distributions during your lifetime. This makes it far easier to calculate the required minimum distribution because you:
  1) Simply divide the prior year-end balance in your retirement account by a uniform distribution period (see Table 1) in order to determine your required minimum distribution amount;
  2) No longer need to irrevocably determine your beneficiary as of your required beginning date;
  3) No longer need to decide whether or not to recalculate your life expectancy each year in determining required minimum distributions; and
  4) No longer need to satisfy a separate "incidental death benefit" rule.

- The regulations permit your required minimum distributions during your

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lifetime to be calculated without regard to your designated beneficiary's age (except when required distributions can be reduced by taking into account the age of a spouse beneficiary who is more than 10 years younger than you).

- The regulations permit your beneficiary to be determined as late as the end of the year following the year of your death. This means that:
  1) You can change designated beneficiaries after the required beginning date without affecting your required lifetime minimum distribution, and
  2) Your beneficiary can be changed after your death, such as by one or more beneficiaries disclaiming their ownership interest or being cashed out.

- The regulations permit the calculation of post-death minimum distributions to take into account your designated beneficiary's single life expectancy or your remaining life expectancy at the time of your death (if no individual beneficiary is named and death occurs on or after the required beginning date), thus allowing distributions in all cases to be spread over a number of years after death.

These new regulations also have the effect of reducing the required minimum distributions for the vast majority of plan participants and IRA owners. This means that your account is likely to benefit from a longer period of tax-deferred growth.

The regulations are mandatory for determining required minimum distributions for calendar years beginning on or after January 1, 2002. For determining minimum distributions from IRAs for calendar year 2001, you may rely on either these rules or on the 1987 proposed regulations.

THE DISTRIBUTION PERIOD

Your required minimum distribution is determined by dividing the prior year-end account balance by the distribution period. For lifetime required minimum distributions, the 2001 proposed regulations provide a uniform distribution period for all owners of plan or IRA assets of the same age, regardless of whether or not a designated beneficiary has been named. The new uniform distribution period table is the old required "minimum distribution incidental benefit" (MDIB) divisor table. The only exception to using this table applies if your sole beneficiary is a spouse who is more than 10 years younger than you. In that case, you are permitted to use the longer distribution period measured by the joint life and last survivor life expectancy table.

The MDIB table (see Table 1) is based on the joint life expectancy of the owner, and a beneficiary assumed to be 10 years younger than the owner, beginning at age 70, and applies regardless of whether a beneficiary is designated.

These new proposed regulations make the calculation easier for people who are now reaching their required beginning date. Furthermore, if you are past your required beginning date, you may adjust your distributions going forward by using the new life expectancy table (Table 1).

The required minimum distribution under the new rules will likely be significantly lower; therefore, you should calculate and compare the required amounts under both the old and the new rules and choose accordingly for 2001 distributions.

EXAMPLE 1

New Rules: If you were born on June 1, 1931, you would reach 70½ on December 1, 2001. If you had $100,000 in your IRA as of December 31, 2000, you'd have to take out at least $3,817 ($100,000/26.2) for 2001, regardless of who your designated beneficiary is. This distribution is required to be made no later than April 1 of 2002. For 2002, your divisor would be 25.3, which is your life expectancy at age 71. Assuming your account had a 0% return and thus an account balance of $96,183 remaining after the last distribution, you would have to take out $3,802 ($96,183/25.3). This distribution must be made no

TABLE 1. THE NEW IRA LIFE EXPECTANCY TABLE

Age	Distribution Period	Age	Distribution Period	Age	Distribution Period
70	26.2	85	13.8	100	5.7
71	25.3	86	13.1	101	5.3
72	24.4	87	12.4	102	5.0
73	23.5	88	11.8	103	4.7
74	22.7	89	11.1	104	4.4
75	21.8	90	10.5	105	4.1
76	20.9	91	9.9	106	3.8
77	20.1	92	9.4	107	3.6
78	19.2	93	8.8	108	3.3
79	18.4	94	8.3	109	3.1
80	17.6	95	7.8	110	2.8
81	16.8	96	7.3	111	2.6
82	16.0	97	6.9	112	2.4
83	15.3	98	6.5	113	2.2
84	14.5	99	6.1	114	2.0
				115 & older	1.8

later than December 31, 2002.

Old Rules: Given the hypothetical situation above, you would have to start the distribution process by designating a beneficiary. Next, you'd have to decide whether to use the single or joint life expectancy table. If your beneficiary was your spouse, who was also age 70 in 2001, the required minimum distribution would be $4,854 ($100,000/20.6); that's because the joint life expectancy of two 70-year-olds is 20.6 years. In this situation, under the old rules your retirement account balances would be paid out more quickly. And you would be faced with the additional burden of having to decide which calculation method (term-certain, recalculation, or hybrid) to use in subsequent years. See IRS Publication 590 for complete joint life expectancy tables.

EXAMPLE 2

New Rules: You were born on June 1, 1931, the same as in Example 1, and your account balance as of December 31, 2000, is again $100,000. However, in this example, your spouse is age 55 in 2001. Your 2001 required distribution based on the new table of factors is $3,817, the same as in Example 1. However, since your spouse is more than 10 years younger than you, you may elect to use a joint life expectancy factor based on your actual ages. This results in a factor of 29.9 and a smaller required minimum distribution of $3,345 ($100,000/29.9).

Old Rules: The joint life expectancy factor for you and your spouse for 2001 would be 29.9, so your required minimum distribution is $3,345. Therefore, the new proposed regulations and the old rules yield the same result (assuming you elect to use the actual joint life expectancy factor under the new rules).

EXAMPLE 3

New Rules: The new rules also give you more planning options. Suppose you were born on June 1, 1931, and named your favorite charity as your IRA beneficiary because your family did not need the money. Under the new rules, the life expectancy would be 26.2, which would generate a distribution of $3,817 ($100,000 / 26.2). In addition, your family would not pay estate tax on this account when you die. The remaining balance passes to the charity as a charitable deduction for your estate.

Old Rules: In contrast, the old rules would have forced you during your lifetime to use the single life expectancy table because a charity could not be a designated beneficiary for minimum distribution purposes. In the single life expectancy table, your life expectancy would be 16, and your distribution from a $100,000 account in 2001 would be $6,250 ($100,000/16), substantially higher than under the new proposed rules.

For the years after the year of your death, the distribution period is generally the remaining "single life expectancy" of your designated beneficiary (see IRS Publication 590 for single life expectancy tables). Your beneficiary's remaining life expectancy is calculated using the age of your beneficiary in the year following the year of your death (reducing the table factor by one in each subsequent year). If there is no designated beneficiary as of the end of the year of your death, and you died on or after the required beginning date, the distribution period is your life expectancy calculated in the year of death (reducing the table factor by one in each subsequent year).

If your spouse is the sole beneficiary at the end of the year following the year of death (and she has not elected to treat the IRA as her own, or has not rolled the IRA proceeds into her own account), the distribution period during your spouse's life is your spouse's single life expectancy. For years after the year of your spouse's death, the distribution period is your spouse's life expectancy calculated in the year of death (reducing the table factor by one in each subsequent year).

IRA REPORTING

Because these regulations substantially simplify the calculation of required minimum distributions from IRAs, IRA trustees can calculate the current year's required minimum distribution for each IRA very early in the year. To improve compliance and further reduce the burden imposed on you and your beneficiaries, under the authority provided in section 408(i), the proposed regulations would require the trustee of each IRA to report the amount of the required minimum distribution from the IRA to you, the IRA owner, or your beneficiary, and to the IRS (at the time and in the manner provided under IRS forms and instructions). This reporting would be required regardless of whether you, the IRA owner, are planning to take the required minimum distribution from that IRA or from another IRA, and would indicate that you are permitted to take the required minimum distribution from any other IRA that you own. This reporting is not due to begin until calendar years beginning on or after January 1, 2002.

CONCLUSION

The 2001 proposed regulations simplify the IRA distribution rules, eliminating many traps. The new rules do not address all potential situations, so the need for distribution planning in both retirement and estate planning, especially for large IRAs, is still very important. You may want to contact your tax or financial planning advisor to assess your unique situation and to determine your best retirement plan distribution strategy. ✦