

ADVANCED MARKETS

IRA Beneficiary Rules After The SECURE Act



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Highlights

The “Setting Every Community Up for Retirement Enhancement” (SECURE) Act was passed on December 19, 2019. In this Athene white paper, we will break down the inherited IRA changes brought about by this Act and help you guide your clients through the process. These changes include:

- ✓ Rules for beneficiaries of IRAs and qualified plans for deaths that occurred on January 1, 2020, and later.
- ✓ Adjustments to the Required Beginning Date (RBD) from age 70 ½ to 72.
 - Note: subsequent legislation pushed back the RBD to 73 beginning in 2023 and 75 beginning in 2033.
- ✓ The following three classes of IRA beneficiaries:
 1. Eligible Designated Beneficiaries.
 - Surviving spouse.
 - A disabled or chronically ill individual (as of the date of death).
 - An individual no more than 10-years younger than the IRA holder.
 - The minor child of the IRA holder.
 2. (Non-Eligible) Designated Beneficiaries.
 - Regulation bifurcates the 10-Year Rule based on the age of the IRA holder at their passing.
 3. Non-Designated Beneficiaries.
- ✓ Regulations for inherited Roth IRAs.
- ✓ How Successor Beneficiaries are impacted by the SECURE Act.

The Old Rules

The SECURE Act applies to deaths occurring on or after January 1, 2020. Therefore, we must not forget the “old rules” for IRA beneficiaries. (For purposes of this whitepaper “IRA beneficiaries” refer to beneficiaries of IRA’s, Roth IRA’s and Qualified Plans, unless otherwise noted.) Pre-2020 we had two types of IRA beneficiaries: designated beneficiaries and non-designated beneficiaries.

Designated beneficiaries were any living, breathing human being who inherited an IRA. Designated beneficiaries pre-SECURE Act were able to “stretch” an IRA and take annual required minimum distributions (RMDs) based on their remaining life expectancy. Those beneficiaries who elected the “stretch” from an IRA holder who passed away prior to January 1, 2020, are grandfathered in and the old rules apply. We will discuss the rules for non-designated beneficiaries later in this whitepaper (*spoiler alert: the SECURE Act did not change the rules regarding non-designated beneficiaries*).

The Required Beginning Date (RBD)

Noted IRA commentator Ed Slott has said since the passage of the SECURE Act and subsequent regulations that RBD now should stand for “really big deal.”

It is essential to know what the actual RBD is. The RBD is the date on which the first RMD is due from an IRA or qualified plan. That date is April 1st the year after the IRA holder turns their qualifying RBD age. That age has changed over the past couple of years due to the SECURE Act and SECURE 2.0. Currently the RBD age is 73 and the first RMD is due April 1st the year after the IRA holder turns 73.

The RBD rules only apply to traditional IRAs and qualified plans, not Roth IRAs. Remember, Roth IRAs do not have a RMD requirement while the Roth IRA holder is alive, therefore there is no RBD for Roth IRAs.



Required Beginning Date = Really Big Deal

The RBD age was:

- 70 ½ – pre-SECURE Act.
- 72 from 2020-2022.
- 73 starting with the enactment of SECURE 2.0 on January 1, 2023.
- Current legislation increases the RBD to age 75 on January 1, 2033.

Three Classes of IRA Beneficiaries

The SECURE Act applies to deaths that occurred on January 1, 2020, and after. The three classes of IRA beneficiaries created by the SECURE Act are: eligible designated beneficiaries, (non-eligible) designated beneficiaries and non-designated beneficiaries.

Understand the **five types of eligible designated beneficiaries**.



1 Class #1: Eligible Designated Beneficiaries

Eligible designated beneficiaries are still able to stretch an inherited IRA based on their life expectancy just as they were pre-SECURE Act. **There are five types of eligible designated beneficiaries:**

- 1 **Surviving Spouse** (The SECURE Act did not change the rules for a surviving spouse; they still have all the inherited IRA options that were available pre-SECURE Act, including treating the IRA as their own).
- 2 **A disabled individual** (disabled as of the date of death of the IRA holder and defined in Internal Revenue Code section 72(m)(7)).
- 3 **A chronically ill individual** (chronically ill as of the date of death of the IRA holder and defined in Internal Revenue Code section 7702(B)(c)(2)).
- 4 **An individual not more than 10-years younger** than the IRA holder (or older).
- 5 **The minor child** of the IRA holder under age 21 (can stretch until they attain age 21, then the 10-year rule applies).

2 Class #2: (Non-Eligible) Designated Beneficiaries

Designated beneficiaries – or non-eligible designated beneficiaries as they are referred to in some places – are living, breathing human beneficiaries who do not qualify as eligible designated beneficiaries. This is the group of beneficiaries most impacted by the SECURE Act with the introduction of the 10-year rule. Designated beneficiaries can no longer stretch an inherited IRA, instead the inherited IRA must be liquidated by December 31 of the 10th year following death.

The 10-Year Rule: Our Original Understanding and Subsequent IRS Regulations

As we originally understood the 10-year rule, there were no annual RMDs for the beneficiary and the only requirement was that the entire inherited IRA must be liquidated by December 31 of the 10th year following death. On February 23, 2022, (26 months after the enactment of the SECURE Act), the IRS introduced regulations that took the industry by surprise and turned the 10-year rule on its head. Spoiler alert: The regulations are now final as of July 18, 2024. The regulations essentially bifurcated the 10-year rule and created two classes of designated beneficiaries. The two classes of designated beneficiaries have different distribution rules based upon the age of the IRA holder on their date of death.

Remember the RBD? Well, now we will see why Ed Slott said it has become a “really big deal.” If the IRA holder died prior to their RBD, then the 10-year rule is applied how we previously understood it with no annual RMD. If the IRA holder died on or after their RBD, then the IRA beneficiary is subject to annual RMDs and the 10-year rule. The rationale applied by the IRS is the “at least as rapidly” rule. The thought process is as follows: if the IRA holder started RMDs, then the beneficiary should be subject to them as well.

IRA Holder Dies Prior to their RBD

- No RMDs.
- Distributions may be made at any time and in any amount during the 10-year period. No 10% penalty for those under age 59 ½.
- The entire inherited IRA must be liquidated by December 31 of the 10th year following death.
- Any money in the account at the end of the 10-year period would be considered a missed RMD subject to penalty.

IRA Holder Dies On or After their RBD

- Annual RMD is required in years 1-9 and the entire account balance must be liquidated by December 31 of the 10th year following death.
- **RMD is based on the life expectancy of the beneficiary. RMDs are calculated just as they were pre-SECURE Act.**
- Any money in the account at the end of the 10-year period would be considered a missed RMD subject to penalty.
- No 10% penalty for those under age 59 ½.



RMD Calculation

Take the age of the beneficiary the year after the IRA holder passes away,

use the single-life table to determine the life expectancy factor,

subtract one from the factor each subsequent year



Final regulations were released on July 18, 2024.

The RMD Requirement under the regulations

Between the issuance of proposed regulations and final regulations, there was confusion about whether the impacted designated beneficiaries needed to take a RMD. Therefore, the IRS was compelled to issue Notices in 2022, 2023 and 2024 granting temporary relief from the missed RMD penalty. IRS Notice 2022-53 (October 7, 2022), IRS Notice 2023-54 (July 14, 2023), and IRS Notice 2024-35 (April 16, 2024) waived the penalty for a missed RMD – essentially eliminating the requirement for those beneficiaries to take the RMD. These notices have not given any indication that the RMDs will need to be made up.

The IRS finalized regulations on July 18, 2024, which confirmed the position of the proposed regulations. Designated beneficiaries that inherit from an IRA holder who died on or after their RBD are subject to annual RMDs **and** the 10-year rule.

Roth IRAs and the 10-year Rule

As mentioned earlier in this article Roth IRA holders do not have a RBD. This is crucial to the application of the SECURE Act rules because Roth IRA beneficiaries are not subject to the bifurcated 10-year rule. If there is no RBD, it is impossible for a Roth IRA holder to die on or after a date that does not exist. Therefore, all Roth IRA holders are deemed to have died prior to the RBD. A designated beneficiary who inherits a Roth IRA is not subject to annual RMDs. They are only subject to the 10-year rule and can liquidate the inherited Roth account at any time and in any amount during the 10-year period ending December 31 of the 10th year following the death of the Roth IRA holder.

3 Class #3: Non-Designated Beneficiaries

Non-Designated Beneficiaries are those beneficiaries who do not have a life expectancy. The SECURE Act did not change the rules for non-designated beneficiaries. How a non-designated beneficiary liquidates an inherited IRA depends upon the age of the IRA holder at death. If the IRA holder died prior to their RBD, then the five-year rule applies. If the IRA holder died on or after their RBD then the inherited IRA can be stretched based on the remaining “ghost” life expectancy of the deceased IRA holder. Please note: a non-designated beneficiary can always elect to take the proceeds in a lump sum. This is often the case when a charity is named as the IRA beneficiary.

Successor Beneficiaries

A successor beneficiary is the beneficiary of an inherited IRA. The SECURE Act had a significant impact on successor beneficiaries and how they must liquidate an inherited IRA.

Pre-SECURE Act the saying was that you could not “stretch a stretch.” The successor beneficiary simply stepped into the shoes of the original IRA beneficiary and continued their stretch. They were not allowed to re-calculate the inherited stretch IRA based on their life expectancy.

Post-SECURE Act you still cannot “stretch a stretch” and you still step into the shoes of the original IRA beneficiary, but now the successor beneficiary is limited by the 10-year rule as well. As outlined below the date of death and age of the original IRA holder are essential to the application of the SECURE Act rules to successor beneficiaries.

Additionally, there is no such thing as an eligible designated successor beneficiary. **All successor beneficiaries are designated beneficiaries.**

The most common non-designated beneficiaries are **charities, estates, and non-qualifying trusts.**



How a successor beneficiary liquidates the inherited IRA is dependent upon when the original IRA holder passed away.



If the original IRA holder passed away prior to January 1, 2020



the successor beneficiary has until December 31 of the 10th year following the death of the inherited IRA holder to liquidate the inherited IRA.



If the original IRA holder passed away January 1, 2020 or later



A successor beneficiary steps into the shoes of the original beneficiary and has whatever remains of the original 10-year period to liquidate the inherited IRA.

The successor in this situation does not get a new 10-year period.

If the original IRA holder passed away prior to January 1, 2020, then the successor beneficiary has until December 31 of the 10th year following the death of the inherited IRA holder to liquidate the inherited IRA.

If the original IRA holder died on or after their RBD, then the successor beneficiary is subject to RMDs and continues the RMDs of the original beneficiary. If the original IRA holder died prior to their RBD and after January 1, 2020, then there would not be an annual RMD requirement.

If the original IRA holder passed away on or after January 1, 2020, then the successor beneficiary steps into the shoes of the original beneficiary and has whatever remains of the 10-year period to liquidate the inherited IRA. Unless the original beneficiary was an eligible designated beneficiary, then the successor has until December 31st of the 10th year following the death of the IRA beneficiary.

There was a gray area that existed for RMDs where the original IRA holder died prior to their RBD (before the enactment of the SECURE Act) or when a successor beneficiary inherits from an eligible designated beneficiary where the original IRA holder died prior to the RBD. In both cases, the original beneficiary started RMDs, but it is possible, due to the wording of the SECURE Act, the successor would not be required to continue those RMDs and would only be subject to the 10-year rule. The final regulations removed this gray area. In all cases where a beneficiary was taking annual RMDs, a successor beneficiary must continue those RMDs. Once RMDs are turned on, they cannot be turned off.

Summary

The SECURE Act made major changes to the liquidation options available to a large group of IRA beneficiaries. The “stretch” IRA is not completely gone, but is limited to a select group of eligible designated beneficiaries.

The 10-year rule has replaced the stretch for designated beneficiaries and whether RMDs are due inside the 10-year rule depends on if the IRA holder died on or after their RBD.

Knowing these rules will help guide your clients through the inherited IRA maze.

IRA BENEFICIARY RULES AFTER THE SECURE ACT

Required Minimum Distribution as defined by Internal Revenue Code Section 401(a)(9).

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