Required Minimum Distributions

SITUATION: We have several former employees who have retired and left their 401(k) account balances in our plan.

QUESTION: When are we required to start distributing money to them from their plan accounts?

ANSWER: In general, retirement plans must make required minimum distributions (RMDs) to retired employees who have reached age 70½ *and* to any current employees who own more than 5% of the company and are age 70½ or older. RMDs also must be paid to beneficiaries of a deceased employee's qualified plan account.

DISCUSSION: More specifically, RMDs must begin by the "required beginning date" (RBD). The tax law provides that the RBD is April 1 of the year following the year a retired employee or a more-than-5% owner turns age 70½. If an employee (other than a 5% owner) continues to work for the sponsoring employer after age 70½, the plan can allow the employee to wait until April 1 of the year after retirement to start taking RMDs.

For beneficiaries of employees who die before their RBD, minimum distributions usually must start on or before December 31 of the year after the year of the employee's death. However, a surviving spouse who is the sole account beneficiary and leaves the money in the plan has the option to wait until December 31 of the year the employee would have turned age 70½.

Your plan must make subsequent RMDs by December 31 of each year.

Basically, an employee's RMDs are calculated each year based on the employee's age using the IRS's Uniform Lifetime Table. A more favorable joint life expectancy table can be used if the employee's spouse is more than 10 years younger than the employee.

For an individual beneficiary designated by an employee who dies before his or her required beginning date, RMDs generally are calculated based on the beneficiary's life expectancy. When the employee has designated more than one beneficiary, the oldest beneficiary's life expectancy should be used. If the employee dies after his or her RBD, the remaining balance must be paid out over the longer of the beneficiary's or the employee's remaining table life expectancy.

COMMENT: Fall is a good time for plan sponsors to review their plans in preparation for making RMDs to retired employees and beneficiaries. If you have questions, please give us a call.