



REQUIRED MINIMUM DISTRIBUTIONS FOR QUALIFIED RETIREMENT PLANS IRC Section 401(a)(9)

Background

A common advantage of retirement plans, such as the 401(k), is the avoidance of paying taxes today. This deferral process allows employees to compound interest in their retirement accounts on money they would otherwise have had to pay to the government in income taxes each year. However, this tax avoidance cannot continue forever—at some point the government expects to collect taxes from your 401(k).

What are Required Minimum Distributions, and when do they begin?

Part of the government's compromise in creating such a tax exemption is the establishment of a date where distribution is required to begin from a participant's retirement account. The triggering event for this date is the Required Minimum Distribution (RMD) which is defined as the minimum amount that a retirement plan account owner must withdraw annually beginning the April 1 of the next year immediately after reaching the last occurring of the following events:

- the participant turns 70 ½; (assuming that the plan participant is not a 5% or more owner) or
- the participant retires, whichever is later.¹

Of note, there are a number of complexities including different rules for RMDs after the death of a plan holder such as distributions made:

- to spouses;
- to other beneficiaries; or
- when there is no designated beneficiary.

What are the penalties for failure to take RMDs?

Failure to follow the RMD schedule could result in major monetary penalties to the retirement account. For example, there is an excise tax of 50% of any money which was required to have been distributed that year.²

It is important to note that the company sponsoring a 401(k) program bears some of the responsibility in ensuring the RMDs occur and that the taxes owed on such income is paid to the government. A company may owe substantial fees to the IRS in penalties for failing to properly manage RMDs.³

What if a company cannot locate a plan participant for the RMD?

Companies are required to take reasonable action to contact and locate all of their current and former 401(k) plan participants. Reasonable action entails such steps as:

- searching employee plan records, public records, and credit reporting agency records;
- Using a commercial locator service; and
- Sending USPS certified mail to last known address.

So long as a company is taking reasonable steps, such as those listed above, to try and locate a missing plan participant, the RMDs do not need to be made and no penalties will occur. Once, if ever, the participant is located, the distributions must be made at that time.⁴

What course of action keeps a company in compliance with the IRS?

A company that finds itself subject to penalties can use the Employee Plans Compliance Resolution System (EPCRS) to make voluntary disclosures and corrections for non-compliance with RMDs.⁵ This EPCRS process requires the company to prove to the IRS that it made a reasonable error which it then took reasonable steps to remedy. After these steps the 50% tax may be waived if the IRS approves the disclosure.⁶

Will all of a single participant's retirement plans trigger RMDs at the same time?

Even if the plan participant triggers RMDs in one plan that does not mean another one of the participant's retirement plans triggers RMDs. A given retirement plan must meet the requirements for RMDs on its own merit. Thus, different retirement plans may have different beginning dates for RMDs.

Don't forget:

- RMDs are regular income.
- RMDs are not eligible for rollover distribution.
- You may continue contributing to your plan once RMDs begin.⁷

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Questions - Please call Luke Novak with Rothschild Investment Corporation at (312) 983-8975.

¹ IRC Section 401(a)(9)(C)

² Treas. Reg. §54.4974-2, Q&A 1.

³ See generally, IRC Rev. Proc. 2016-51

⁴ IRC Rev. Proc. 2016-51 § 6.02(5)(d)

⁵ IRC Rev. Proc. 2016-51

⁶ 26 USC § 4974(d)

⁷ See generally, Ferguson et al. Frequently Asked Questions ("FAQ") About Required Minimum Distributions, Ice Miller, accessible at: [https://www.icemiller.com/ice-on-fire-insights/publications/frequently-asked-questions-\(-faqs-\)-about-required/](https://www.icemiller.com/ice-on-fire-insights/publications/frequently-asked-questions-(-faqs-)-about-required/)