05.03.24 I FINANCIAL PLANNING

Navigating Required Minimum Distributions for Inherited IRA Accounts in 2024

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The SECURE Act and SECURE Act 2.0 have reshaped the financial landscape for retirees and taxpayers. Many individuals continue to grapple with comprehending the latest regulatory shifts as it relates to Inheriting IRAs. The IRS hopes to clarify these questions with their latest release.

INHERITING AN IRA PRE-SECURE ACT (DEATHS PRIOR TO JANUARY 1, 2020)

Prior to the SECURE Act, there was very little confusion regarding inheriting an IRA. Similar to taking RMDs when alive, once a tax-deferred IRA was inherited, the non-spouse beneficiary could "stretch" distributions over their own life expectancy, allowing for smaller RMDs and potential tax advantages. This option provided beneficiaries with greater flexibility in managing the inherited IRA assets and tax implications.

INHERITING AN IRA POST-SECURE ACT (DEATHS POST TO JANUARY 1, 2020)

Most non-spouse beneficiaries are now mandated to completely distribute their inherited IRA within a 10-year period, commonly referred to as the 10-year rule. This 10-year rule applies regardless of the beneficiary's age or life expectancy. Exceptions for beneficiaries where "stretch" distributions are still applicable include surviving spouses, minor children of the account owner (until they reach the age of majority), disabled individuals, and individuals not more than 10 years younger than the deceased account owner. Failure to comply with the new regulations may result in an excise tax of 25% of the balance that should have been withdrawn, or 10% if corrected within two years, starting January 1st, 2025.

STRATEGIC PLANNING: CASE STUDY

Jane (age 85) and John (age 90) are married with one child, Jeffrey (age 55). John passed away years ago (pre-2020) and his Traditional IRA was rolled into Jane's IRA. Since Jane and John are married, Jane could continue to take "stretch" distributions from John's IRA. Jane passed away January 1, 2024, leaving Jeffrey her IRA with a balance of $1,000,000. Prior to the SECURE Act, Jeffrey could have taken annual "stretch" distributions over the course of his lifetime (~$34,000/year). Under the new SECURE Act legislation, he'll keep receiving "stretch" RMD payments for the first nine years. However, by the end of the tenth year, he'll need to take a lump sum distribution to close out the account. These distributions will be subject to taxation at Jeffrey's income tax rate, resulting in a substantial tax liability a decade later.

IN CONCLUSION:

Beginning January 1st, 2025, the IRS will start enforcing penalties for annual RMD installments for inherited Traditional or Rollover IRAs associated with non-spouse individuals. It is important to note that this does not impact inherited Roth IRA accounts. This delay allows you the opportunity to strategize and navigate the intricacies of these new changes and their downstream impact for future heirs. We encourage all clients who may have recently Inherited IRAs accounts, will be receiving IRAs as a beneficiary or bequeathing IRAs to discuss these latest updates with your advisor to see how it may impact your situation.

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