...ADVISOR INSIGHTS

How the 10-Year RMD Rules Work for Inherited IRAs

Rules work differently for each class of beneficiary.

Denise Appleby

Mar 21, 2023

Beneficiaries of IRAs and other tax-deferred retirement accounts must take required minimum distributions. The class in which a beneficiary falls determines the RMD rules that apply to them. One of these options is the 10-year rule. When the 10-year rule applies, the inherited account must be fully distributed by the end of the 10th year after the account was inherited. In some cases, annual RMDs must also be taken.

10-Year RMD Rule Background

Limiting designated beneficiaries to the 10-year rule is one of the most impactful changes made by the Setting Every Community Up for Retirement Enhancement Act of 2019, also known as Secure 1.0, which was signed into law on Dec. 20, 2019, as part of the Further Consolidated Appropriations Act, 2020. Before Secure 1.0, a designated beneficiary could take distributions over their *applicable* life expectancy. In addition, when the designated beneficiary died, their successor beneficiary could continue distributions over the designated beneficiary's remaining life expectancy.

Effective for accounts inherited after 2019, designated beneficiaries can no longer stretch distributions beyond 10 years after the IRA owner or plan participant's death. In addition, a successor beneficiary can no longer stretch distributions for more than 10 years after the original beneficiary's death.

Beneficiary Classes

There are four primary classes of beneficiaries:

- **Designated beneficiary**: A designated beneficiary is a person. A trust that qualifies as a see-through trust—thus allowing the life expectancy of a beneficiary of the trust to be used for RMD purposes—is also a designated beneficiary.
- **Eligible designated beneficiary:**Created under Secure 1.0, an eligible designated beneficiary is a designated beneficiary who, as of the date of the participant's death, is either of the following: a) the surviving spouse of the participant, b) a child of the participant who has not yet reached the age of 21; c) disabled; d) chronically ill; or e) an individual not described in any of the above who is not more than 10 years younger than the participant. An eligible designated beneficiary may take distributions over the entire length of their life expectancy unless the 10-year rule applies. (See "10-Year Rule Number One: When the Participant Dies Before Their RBD"below.)
- **Nondesignated beneficiary***:* A beneficiary who does not meet the requirements to be a designated beneficiary.
- **Successor beneficiary**: A beneficiary who inherited the account after the original beneficiary's death.

Except for nondesignated beneficiaries, all beneficiaries *could* be subject to one of the three 10-year rules.

Note, I will not cover the following beneficiary types in this article:

- **Nondesignated beneficiary***:* A nondesignated beneficiary does not qualify as a designated beneficiary. The 10-year rule does not apply to nondesignated beneficiaries.
- **Spouse beneficiary***:* The options available to a spouse beneficiary extend beyond the scope of this article.
- **Trust beneficiary***:* The complexities of a trust beneficiary are beyond the scope of this article.

The Importance of the Required Beginning Date

Which of the three 10-year rules applies to a beneficiary depends on whether the participant died before their required beginning date, or RBD, and the beneficiary class under which they fall. The RBD is April 1 of the year that follows the year the participant reaches their applicable RMD age.

The applicable RMD ages are:

- 70½ for those who reach age 70½ before 2020,
- 72 for those who reach age 70½ after 2019 and reach age 72 before 2023,
- 73 for those who reach age 72 after 2022 and reach age 73 before 2033, and
- 75 for those who reach age 74 after 2032.

The applicable RMD age can be deferred past these ages until retirement for a participant in an employer-sponsored retirement plan, if the plan's terms allow such a deferral.

Let's now dive into the three 10-year rules.

10-Year Rule Number One: When the Participant Dies Before Their RBD
Under this 10-year rule, distributions are optional for the nine years after the participant's death, and the account must be fully distributed by the end of the 10th year.

This 10-year rule is the only option available to a designated beneficiary. On the other hand, it is one of two options available to an eligible designated beneficiary, the other being the life expectancy option.

Under the life expectancy option, the eligible designated beneficiary may take distributions over their entire life expectancy, beginning by Dec. 31, following the year the participant dies.

Special rule for minors: If the eligible designated beneficiary is the minor child of the participant and the life expectancy rule applies, distributions would switch from the life expectancy rule to a combination of the 10-year rule and the life expectancy rule when the minor reaches age 21. Under this combination, annual RMDs would be taken over the minor's life expectancy, and the account must be fully distributed by the end of the 10th year after the child reaches age 21.

Planning tip: For an eligible designated beneficiary, this 10-year rule may apply either by election or under the default terms of the governing plan document.

If the assets are held under a qualified plan document that allows only the 10-year rule for an eligible designated beneficiary, this limitation can be overridden by moving the assets to a beneficiary IRA that permits distributions over the beneficiary's life expectancy. This move must be done as a direct rollover by Dec. 31 of the year following the year the participant dies.

10-Year Rule Number Two: When the Participant Dies on or After Their RBD

Under this 10-year rule, annual RMDs must be taken over the life expectancy of the designated beneficiary beginning by Dec. 31 of the year that follows the year the participant dies. In addition, the inherited account must be fully distributed by Dec. 31 of the 10th year following the year the participant dies.

This 10-year rule applies only to a designated beneficiary.

Special rule for minors: If the beneficiary is an eligible designated beneficiary because they are a minor child of the participant, distributions would be taken over the child's life expectancy, and the account must be fully distributed by the end of the 10th year after the year the child reaches age 21.

Planning tip: If the participant did not take their RMD for the year they died, their beneficiaries must take that RMD. This RMD is calculated as if the participant lived through to the end of the year.

10-Year Rule Number Three: When the Eligible Designated Beneficiary Dies

This 10-year rule applies to a successor beneficiary who inherits a retirement account after 2019 from an eligible designated beneficiary taking distributions over their applicable life expectancy. For this purpose, a designated beneficiary is considered an eligible designated beneficiary if they:

- Inherited the retirement account before 2020,
- Were taking distributions under the life expectancy method, and
- Died after 2019.

Under this 10-year rule, the successor beneficiary must continue taking annual distributions over the life expectancy that applied to the eligible designated beneficiary. In addition, the account must be fully distributed no later than the end of the 10th year following the year of the eligible designated beneficiary's death.

IRS Waives Excise Tax for 10-Year Rules Two and Three

Language from Secure 1.0 led many to believe distributions were optional until the 10th year for all beneficiaries subject to the 10-year rule. However, the proposed RMD regulations explained that annual RMDs were also required under 10-year rule number two and 10-year rule number three.

Generally, a beneficiary who fails to take an RMD for a year owes the IRS an excise tax on any RMD shortfall. Because of confusion about how the 10-year rules work for beneficiaries that fall under 10-year rules number two and three, the IRS provides an automatic waiver of this excise tax for any of these beneficiaries who failed to take their RMDs for 2021 and 2022.

Planning Tips for Advisors

One of the first steps in advising a beneficiary about their distribution options is determining whether they are a designated beneficiary, an eligible designated beneficiary, a nondesignated beneficiary, or a successor beneficiary.

Another important determining factor is whether the participant died before their RBD.

Equally important is whether the primary beneficiary was subject to the 10-year rule (or five-year rule if the participant died before 2020). In those cases, a successor beneficiary must fully distribute the inherited account at the end of the original 10-year or five-year period that applies to the primary beneficiary. Reminder: 2020 is not counted for the five-year period because the Cares Act waived RMDs for 2020.

Creating a profile for each beneficiary will help ensure you get the data needed to provide correct information. To that end, a practical solution is using a standard form to collect the necessary information.