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## Immediate Risk for Distributions for Older Participants

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There is an immediate risk of loss of monies and litigation to plan sponsors and participants for terminated participants who take a distribution on or after January 1, 2020. Attention is required at this time.

To prevent the risk, plan sponsors should consider delaying all distributions until such time the matter can be addressed. This mostly affects participants who will attain age 70 ½ after 2019, or who are already 70 ½ and who have not yet terminated employment.

### BACKGROUND

Prior to the just-enacted SECURE Act, a participant is required to receive a taxable, non-rolloverable required minimum distribution ("RMD") upon attaining age 70 ½, or in many circumstances upon the later of age 70 ½ and retirement. After the SECURE Act, participants who were not yet 70 ½ as of December 31, 2019 will not take their first RMD until the year in which they turn 72 (or if the plan allows, also after they retire). Participants whose first RMDs were due for the 2019 year (because they attained age 70 ½ in 2019 or earlier) or earlier are not affected by this change. Note that RMDs due by April 1, 2020 are for 2019, not 2020 for non-deceased participants. Also note that RMDs starting before 2019 likely are still due in 2020.

Recordkeepers will need time to program for this, but the challenge for now is *not* paying RMDs in 2020 and later that are *not* due before then.

Because of the law change, an affected participant might, and perhaps likely will, suffer an irrevocable tax loss (depending on possible, perhaps future legal guidance). A participant will pay taxes, and perhaps look at the employer for reimbursement, on amounts that could have avoided tax by rollover.

### TAX LOSS

The tax loss arises because plan sponsors report to participants distributions that are RMDs, and must provide a special (Section 402(f)) tax notice, and RMDs when distributed cannot be rolled over to an IRA or other tax-favored plan. An RMD must be taxed. If an older participant receives a lump sum or partial distribution and some of that distribution constitutes an RMD, the RMD portion may not be rolled over – a rollover would give rise to tax penalties and consequences. The problem exists because a participant in 2020 who receives a distribution might understand that there is an RMD that may not be rolled over, but which under the new law indeed may be rolled over and avoid taxation.

One example: a participant terminates employment in 2020, elects a lump sum distribution in 2020, and attains age 70 ½ in 2020. Under the law prior to 2020, the participant could not roll over her entire lump distribution because the RMD portion was not rolloverable. Now, however, that portion which would be an RMD is not an RMD, because the participant is not yet age 72. The participant can in fact avoid immediate taxation on what would be the RMD by timely rolling it in 2020.

How will participants know this in time, for example, a distribution occurring in January, February, etc.?

Plan providers will need to change their programming software to reflect the law change, more specifically to recode what would have been an RMD under the old law but is no longer an RMD in 2020. Because of the very late enactment of the SECURE Act and apparent no thought given to its timing impact, no programming software could have been changed in time for distributions occurring on January 1, 2020, or after, and some time is needed before programming is changed to properly reflect the distribution's tax treatment. Until the programming is changed, all lump sum or partial distributions that contain RMDs will be reported as not being eligible for rollover, when in fact they may be.

## IMMEDIATE ACTION STEPS

Plan sponsors should immediately take several steps:

1. Bring this to the attention of your TPA and recordkeeper.

2. Likely postpone all distributions until you and the TPA/recordkeeper can identify the older participants who will be affected by this change.

3. Convey to participants this change in law such that the participant may understand it and avoid taxation even though the information from the recordkeeper/TPA may provide conflicting information.

4. Contact your ERISA attorney or trusted ERISA advisor for specific guidance.

5. Finally, life expectancies also have changed for RMD calculations. Again, prudence dictates the law be examined without delay.

A thank you and credit given: Our firm produces the monthly journal *The 401(k) Advisor* with publisher Wolters Kluwer. This issue and the gravity of it was brought to our attention courtesy of Adrienne Robertson from Transamerica, a contributing author to *The 401(k) Advisor*. Attached is a copy of her article.

For additional information or if you have questions, please contact Jeffrey Johns (jjohns@erisalawgroup.com) at 913.647.7552 or Jeffery Mandell (jeff@erisalawgroup.com) at 208.342.5522.

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The full text of the report can be accessed at: *https://www.usatoday.com/story/money/2019/09/23/401-k-americans-gen-x-race-build-retirement-savings/2379769001/*. Paul Davidson. USA Today. Published September 23, 2019.

## LAST WORD ON 401(k) PLANS

# RMD Challenge – The SECURE Act

*Adrienne Robertson*

The eleventh hour passage of the SECURE Act, with no modification to the effective dates of its provisions, has left plan sponsors and their recordkeepers with a variety of administrative challenges around the provisions that became effective as of January 1, 2020. One of the more time sensitive of these challenges relates to the change in the required beginning date for required minimum distribution (RMD) provisions. Under the SECURE Act, participants who were not yet 70-1/2 and terminated as of December 31, 2019 will not need to take their first RMD until the year in which they turn 72 (and, if required by the plan, are terminated). Participants whose first RMDs were due for 2019 or earlier are unaffected by this change. Consequently, no *new* RMDs will be due for 2020 (noting that RMDs payable by April 1, 2020, are for 2019). Recordkeepers will need some time to program for this, but, since no new RMDs will be due this year, it should not be a problem, right?

The challenge will not be correctly paying RMDs under the new age rule when they come due, it will be *not* paying RMDs that are *not* due before then. Take, for example, a participant who is turning 70-1/2 in 2020, terminates employment in 2020, and elects to take a full distribution of his or her account balance before recordkeepers have completed the reprogramming of their systems for this change. Normally, to comply with applicable law, recordkeeping systems are programmed to pay out the first portion of a distribution as an RMD when a distribution is paid out in a year in which an RMD is due and, prior to the SECURE Act's passage, 2020 would have been an RMD distribution year for this participant. As a result, recordkeeping systems will automatically code portion of the participant's distribution as his or her first RMD; it will be improperly treated as ineligible for rollover and it will not be subject to the 20% withholding that should properly apply to an eligible rollover distribution that is not rolled over. This is an issue for participants, who will be taxed on amounts they could have rolled over, as well as for the payor (in most cases, the plan's recordkeeper), who might be subject to underwithholding penalties.

Unless the IRS releases nonenforcement relief or other clarifying guidance, plan sponsors may want to ask their recordkeepers if there are any manual processes or system overrides that could be utilized until their systems are reprogrammed. In addition, a communication to any such participants may be in order, to inform them that any money distributed and coded as an RMD is in fact eligible for rollover.

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