Pension ANALYST
COMPLIANCE BULLETIN

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IRS Revises Portion of Minimum Distribution Rules For Defined Contribution Plans

In 2002, the IRS published final rules relating to Minimum Required Distributions (MRDs) from qualified defined contribution plans and 403(b) programs. These rules contain a special provision for calculating death benefit MRDs when a participant has designated multiple beneficiaries. The IRS has now revised this rule, to ease plan administration.

General Rule

In general, when a participant dies before his Required Beginning Date (RBD) and has designated multiple beneficiaries, the oldest beneficiary's life expectancy will determine the distribution period.

For example, Donald names his three nephews, Harry, David and Louis, as joint beneficiaries under the Deptford Company's 401(k) Plan. Donald dies before his RBD, when Harry is age 35, David is age 38, and Louis is 40 years old. Louis' life expectancy of 43.6 years will be used to determine the distribution period for Donald's death benefit, which will be paid in three separate portions to Harry, David and Louis.

Separate Account Exception

If separate accounts are established for multiple beneficiaries, each beneficiary's own life expectancy will be used to determine the distribution period for his portion of the death benefit.

If the Deptford Company Plan establishes separate accounts for Harry, David and Louis, Harry's portion of the death benefit will be paid out over 48.5 years. David's portion will be paid out over 45.6 years. Only Louis' portion will be paid out over 43.6 years.

Original Timing Rule

Under the 2002 final rules, this separate account exception could only be applied for years after the calendar year in which the separate accounts were established, or date of death, if later. If a participant died late in a calendar year, separate accounts often could not be established until the following calendar year. As a result the distributions to all beneficiaries for the first year after the participant's death would have to be based on the life expectancy of the oldest beneficiary.

New Timing Rule

Under the revised rule, which is effective immediately, the separate account exception can be used for the first year after the participant's death if the separate accounts are established by December 31 of the year following the participant's death.

For example, Donald dies on December 18, 2004, before reaching his Required Beginning Date. The Deptford Company Plan is not notified of his death until January 5, 2005. At that time, the Plan establishes separate accounts for Harry, David and Louis. The payments that must be made to these beneficiaries by December 31, 2005, may be based on each individual's own life expectancy. Under the old rule, all of the 2005 payments would have had to be based on Louis' life expectancy, resulting in larger payments being made to Harry and David, because the separate accounts were not established by December 31, 2004.

No Plan Amendments Required

At this time, it appears that no plan amendments are required to take advantage of this revised rule. Most plan sponsors have adopted the final MRD rules by adopting either an IRS model amendment or an amendment patterned after the IRS model amendments provided in Revenue Procedure 2002-29. Those amendments do not address the specific rules for making payments to multiple designated beneficiaries. As a result, the separate account exception may be applied operationally under most plans.