Required distributions from retirement accounts: Planning strategies for advisors.

By Christopher R. Hoyt, JD

For financial professionals and attorneys advising high-net-worth clients, understanding the rules and strategies around required minimum distributions (RMDs) is crucial for tax-efficient planning and wealth preservation. These distributions impact both account owners during their lifetimes and beneficiaries following the account owner's passing. Here's a clear guide on the key points and strategic opportunities related to RMDs, with an emphasis on leveraging life insurance as a holistic, tax-saving solution.

Congress permits people to accumulate large amounts of wealth in their tax-sheltered retirement accounts. But eventually those assets must be distributed, or else there will be a 25% penalty. RMDs must be made from individual retirement accounts (IRAs) and from qualified employer retirement plans (QRPs), which include 401(k) plans, profit sharing plans, and stock bonus plans. Roth accounts [Roth IRAs, Roth 401(k), Roth 403(b) and Roth 457(b)] qualify for more advantageous RMD rules than traditional taxable accounts.

Although contributions to Roth accounts don't qualify for income tax deductions, distributions of the Roth account's investment income will be tax-free if two tests are met: the distribution is made (a) after the account owner has had a Roth account for at least five years, and (b) after age 59½ (though there is no age requirement when inheriting a Roth account).

Lifetime Required Minimum Distributions

Roth accounts

There are no lifetime RMDs from a person's own Roth account at any age. After an individual's death, the Roth account must generally be liquidated by the end of the tenth year after death.

Traditional taxable accounts: RMDs begin at age 73

RMDs must be made to an IRA owner each year, beginning in the year that the IRA owner attains age 73. Failure to receive an RMD triggers a 25% penalty on the amount that was not distributed.

The same rule applies to qualified employer retirement plans (QRPs), except that RMDs are not required from QRPs during those years that an employee continues working after age 73 (provided that the employee owns less than 5% of the business).

Instead, the RMD requirement begins in the year that the employee separates from service. Note that RMDs must still be made from IRAs beginning at age 73, even when a person is working full time. If an individual fails to receive the distribution in this first year, the penalty can be avoided if the distribution is received in the next year at any time before the required beginning date (before April 1 of the following year).

If someone has multiple IRA and QRP accounts, the RMD should be computed separately for each account. The RMD must be distributed separately from each QRP account [including from a 403(b) or a 457(b) account]. There is, however, an administrative advantage available with IRAs: The total amount of the RMDs from all IRAs may be distributed from a single IRA. This can be particularly beneficial when some IRAs hold illiquid assets and others have liquid assets.

The amount of each year's RMD is determined by the Uniform Lifetime Table (*see below*). The sole exception is that there can be smaller RMDs when an IRA owner is married to someone who is more than 10 years younger. When that younger spouse is the sole beneficiary of the account, there are smaller RMDs based on the joint life expectancy of the couple. The computations for such married individuals are available in IRS Publication 590-B.

The percentage of retirement assets that must be distributed from a retirement account gradually increases each year as the IRA owner ages. There are two steps to determine each year's RMD:

> **Step 1:** Determine the value of the investments in the account on the last day of the preceding year (December 31);
>
> **Step 2:** Multiply the value of those investments by the percentage in the table that is next to the age that the IRA owner will be at the end of the year. This is the minimum amount that must be distributed to avoid the 25% penalty.

Example: *Isabel Ringing had $100,000 in her only IRA on the last day of the preceding year. She will be 80 years old*

UNIFORM LIFETIME DISTRIBUTION TABLE

Age	Payout		Age	Payout		Age	Payout		Age	Payout
70	-0-%		80	4.95%		90	8.27%		100	15.63%
71	-0-%		81	5.19%		91	8.78%		101	16.95%
72	-0-%		82	5.44%		92	9.26%		102	17.86%
73	3.79%		83	5.69%		93	9.91%		103	19.24%
74	3.93%		84	5.96%		94	10.53%		104	20.41%
75	4.07%		85	6.25%		95	11.24%		105	21.74%
76	4.22%		86	6.58%		96	12.05%		106	23.26%
77	4.39%		87	6.95%		97	12.83%		107	24.39%
78	4.57%		88	7.36%		98	13.70%		108	25.65%
79	4.77%		89	7.76%		99	14.71%		109	27.03%

[Table computed from Uniform Lifetime Table - Table 2 to Reg. Sec. 1.401(a)(9)-9(c) (rounded up)]

at the end of this year. She must receive at least $4,950 during the year to avoid a 25% penalty (4.95% x $100,000).

RMDs from inherited accounts

Retirement accounts of individuals who died after 2019 must generally be liquidated by the last day of the tenth year that follows the year of death. For example, if an individual died on any day in the year 2025, that person's retirement account musts be empty on December 31, 2035, or else the remaining balance will be subject to a 25% penalty.

There are circumstances when amounts may be distributed penalty-free for more than 10 years, or that the mandatory distribution period may be even less than 10 years. For simplicity, this article will focus only on the planning strategies for the 10-year rule (e.g., when children are the beneficiaries), and the special advantages that are available to a surviving spouse.

RMD in the year of death

In the year that an IRA owner dies, the RMD continues to be the RMD that was required when the person was alive. Thus, in the example above, if Isabel Ringing died in the year that she was going to turn age 80, at least $4,950 would need to be distributed from the IRA to avoid the 25% penalty. If less than $4,950 had been distributed to Isabel that year, the remaining amount should be distributed to the beneficiary(ies) of the IRA in order to avoid the penalty.

The tax regulations give some leeway if the payment was not made to the beneficiaries in the year of death. As long as the amount is distributed to the beneficiary(ies) before the end of the following year, the 25% penalty can be avoided. This exception can be particularly helpful when someone dies in November or December, and there are much more important things that need to be done than to determine whether that year's RMD had been distributed.

Surviving spouse can do a rollover

A surviving spouse who is the beneficiary of a retirement account has an important option that no other beneficiary has: the ability to rollover the assets in the deceased spouse's account into their own IRA. Such rollovers are very common, and they usually produce the greatest tax advantages. Since the account is now the spouse's IRA, the surviving spouse will be subject to the lifetime RMD rules described above.

One situation when a surviving spouse might delay a rollover is when she or he is under age 59½. Taxable distributions from one's own retirement accounts before that age are subject to a 10% penalty, but distributions from inherited accounts are exempt from that penalty at any age. The spouse can leave some assets in the deceased spouse's account and receive distributions from that account without incurring the 10% penalty. After attaining age 59½, the assets can be rolled over to an IRA.

The 10-Year Time Limit

Inherited Roth accounts

If a person inherited a Roth account, there are no RMDs until the last day of the tenth year. Consequently, the best tax-planning strategy for inherited Roth accounts is to avoid receiving any distributions over the 10-year time period to allow the greatest accumulation of tax-free investment income.

Inherited taxable accounts

Even though taxable accounts must be fully liquidated at the end of 10 years, in most cases there also will be RMDs in each of the first nine years. Whether or not RMDs are required depends on whether the original account owner died before or after the required beginning date (described above). Since most people die after age 73, most inherited taxable retirement accounts will have an annual RMD. The rules are:

- If the retirement account owner died *before* the required beginning date, there is no RMD until the last day of the 10th year.
- If the retirement account owner died *after* the required beginning date, the 2024 final regulations require an RMD in each of the nine years that follow the IRA owner's death, and then full liquidation of the account in the 10th year. Each year's RMD is computed based on the beneficiary's remaining life expectancy in the year after the account owner's death.

Planning for Large Inherited Taxable Accounts

If the inherited retirement account holds a small balance, then stretching distributions over 10 years shouldn't pose serious income tax problems. But if the retirement account holds millions of dollars, it would be smart to undertake strategies that will reduce the income tax that will be paid upon distributions.

STRATEGIES DURING THE RETIREMENT ACCOUNT OWNER'S LIFETIME

Roth conversions:

With a Roth IRA conversion, a person can move taxable assets in a traditional IRA into tax-free assets in a Roth IRA.

The conversion triggers taxable income, but there is no 10% penalty on a Roth conversion when the IRA owner is under age 59½. The greatest income tax savings occur if the Roth IRA conversion takes place in a year when a person is in a lower income tax bracket than the tax bracket that would be in place in the year of a future distribution. This can occur if the account owner lives in a state that does not impose an income tax, but the beneficiaries (e.g., children) live in states that do impose income taxes.

Once the assets are in a Roth IRA, the individual benefits from avoiding lifetime RMDs and by having all withdrawals be exempt from income tax. The beneficiaries will benefit by inheriting a Roth IRA that will have no annual RMDs, thereby permitting the investment income to compound tax-free within the Roth IRA for 10 years.

Add more beneficiaries:

For example, a widowed individual might have two children and four grandchildren. Rather than simply naming the two children as beneficiaries, consider naming all six individuals. That way the taxable income from the inherited IRA can be spread over 60 income tax returns over the 10-year period instead of just 20 income tax returns.

The "kiddie tax" can apply to income received by dependents under the age of 19, but with a 10-year liquidation span many of them will be past that age at some point.

Of course, if the IRA owner is so wealthy that there will likely be a federal estate tax liability, then there are likely better assets to leave to grandchildren when planning for the generation-skipping transfer tax.

After age 59½ - Lifetime income tax bracket management:

Withdrawals from retirement accounts should generally be avoided before age 59½ because they are subject to a 10% penalty. After age 59½, individuals can reduce the balances in their accounts by receiving distributions.

Since the distributions generate taxable income, withdrawals should be structured to minimize the income tax cost. From a historical perspective, federal income tax rates are currently "on sale." In 2025, a married couple can have nearly $400K of taxable income (nearly $200K for a single person) before crossing over from the 24% marginal income tax rate to the 32% rate.

Thus, one strategy is to withdraw whatever amounts will get their taxable income up to these thresholds. The maximum federal income tax liability will only be 24%. Then, accumulate the after-tax amounts in a tax-advantageous manner. These accumulation vehicles include:

- Making Roth IRA conversions (described above) from taxable IRAs.
- Contributions to Section 529 college savings plans for children and grandchildren (the investment income is tax-free if used for qualified education expenses).
- Life insurance, especially if the taxpayer will be subject to the federal or a state estate tax. The life insurance policy and proceeds can be excluded from the

estate with, for example, an irrevocable life insurance trust (ILIT). There are no RMDs from a life insurance policy.

After age 70½ - Qualified charitable distributions (QCDs):

After age 70½, an IRA owner should make all of their charitable gifts from their IRA. The QCDs are excluded from their taxable income, count toward satisfying the annual RMD requirement, and will also reduce the balance accumulated in large taxable IRAs.

Name a charity as the beneficiary of some or all of the retirement assets

The tax savings will be greatest for individuals who are wealthy enough that their estates will be subject to federal and/or their state estate tax. The charitable estate tax deduction reduces the estate tax liability, and the tax-exempt charity can apply the entire amount to its charitable purpose without any reduction for income taxes.

STRATEGIES FOR NON-SPOUSE BENEFICIARIES WHO INHERIT LARGE RETIREMENT ACCOUNTS

Before the SECURE Act shortened the withdrawal period to 10 years, people who inherited an IRA could easily stretch distributions over their life expectancy (a “stretch IRA”). The inherited IRA could continue to defer income taxes until the beneficiary attained age 83 (at least). The strategy then was: “defer, defer, defer!” Today, only a few beneficiaries qualify for such stretch treatment.

Instead, current planning strategies for large inherited accounts focus on income-tax planning for large amounts of taxable income that will be received over a 10-year period.

Deferring a massive amount of taxable income to the tenth year will subject most of that income to the highest income tax rate. Instead, beneficiaries should consider withdrawing large amounts each

year (e.g., 10% of the account balance) to reduce the accumulation in the retirement account that will get hit with the highest income tax rate in the tenth year.

Consequently, for large retirement balances, consider these strategies.

1. Plan to use taxable distributions from inherited retirement accounts for living expenses over the 10-year period, thereby permitting other inherited assets to be invested for long-term growth.
2. If the beneficiary hadn't contributed the maximum amount to a retirement account at work ($23,500 to a 401(k) in 2025 ($31,000 if over age 49; $34,750 if between ages 60 and 63)), then take full advantage of that opportunity and increase withdrawals from the inherited IRA to cover the larger contributions. Consider making after-tax contributions to a Roth 401(k), which effectively puts more dollars into a tax-sheltered and tax-free environment.
3. Use the same income-tax management strategies described above for IRA owners. Beneficiaries can use these strategies at any age, since distributions from inherited retirement accounts are not subject to the 10% penalty.
   - Roth IRA conversions of inherited QRP accounts (inherited taxable IRAs don't qualify for a Roth conversion; inherited QRPs do).
   - Roth IRA conversions of the beneficiary's own IRAs .
   - Contributions to Section 529 college savings accounts.
   - Life insurance. There are no RMDs from a life insurance policy.
   - Making Roth IRA conversions (described above) from taxable IRAs.

In conclusion

To ensure clients receive the most tailored and effective financial strategies, collaboration with experienced insurance professionals is essential. Partnering with experts in a holistic approach helps clients understand how to minimize their tax liabilities, maximize the advantages of their retirement accounts, and make a lasting impact for their beneficiaries.

About the author.

Christopher R. Hoyt, JD, is a Professor of Law at the University of Missouri Kansas City School of Law where he teaches courses in the area of federal income taxation and business organizations. Professor Hoyt has served as the Chair of the American Bar Association's Committee on Charitable Organizations (Section of Trusts and Estates) and is on the editorial board of Trusts and Estates magazine. He is an ACTEC fellow, has been designated by his peers as a "Best Lawyer," and was elected to the Estate Planning Hall of Fame by the National Association of Estate Planners & Councils. He is a frequent speaker at legal and educational programs and has been quoted in numerous publications, including *The Wall Street Journal*, *Forbes*, *MONEY* magazine, *The New York Times*, and *The Washington Post*.