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IRS Issues Final Life Expectancy Regulations

On November 12, 2020, the IRS published final regulations updating life expectancy tables that are used for required minimum distributions (RMDs) and for other purposes. These new tables reflect an increase in life expectancies since the last tables were issued nearly 20 years ago. Although the updated tables do not apply until distribution years beginning in 2022, financial professionals should learn how the new life expectancy figures may affect their clients and should assess how their administrative systems will accommodate the changes.

Background

Two years ago, President Trump issued Executive Order 13847, which (among other things) directed the IRS to examine the life expectancy tables and to "determine whether they should be updated to reflect current mortality data and whether such updates should be made annually or on another periodic basis." On November 8, 2019, the IRS published proposed regulations in response to the executive order. The IRS received numerous comments, but the only substantial change made in creating the final regulations was pushing back the applicability date to the 2022 calendar year.

Internal Revenue Code Section (IRC Sec.) 401(a)(9) and associated RMD regulations require "employees" to begin distributing their accumulated retirement assets by their required beginning date. (In this article, we will use the term "employee" because that is the term found in the Internal Revenue Code. It includes qualified plan participants, IRA owners, and all those who must take RMDs (e.g., beneficiaries).) The RMD rules help ensure that employees start taking distributions, and they permit payments over their life expectancy to avoid outliving their retirement savings. The IRS life expectancy tables determine the distribution period over which defined contribution-type retirement plans must be paid. The regulations specifically apply to RMDs taken from

- qualified trusts (such as a 401(k) trust);
- individual retirement accounts and annuities described in IRC Secs. 408(a) and (b);
- eligible deferred compensation plans under IRC Sec. 457; and
- IRC Secs.403(a) and §403(b) annuity contracts, custodial accounts, and retirement income accounts.

The life expectancy tables determine the distribution period for RMDs. The final regulations revise the three life expectancy tables found in Treasury Regulation (Treas. Reg.) 1.401(a)(9)-9. The *Uniform Lifetime Table* is used to determine the distribution period for those employees who must take RMDs during their lifetime. This table begins at age 72, which is the age at which RMDs must first be calculated under the SECURE Act rules. The distribution periods listed are simply the joint life expectancy of the employee at a certain age and a beneficiary who is exactly 10 years younger. Years ago, the IRS simplified the RMD process by allowing all employees—regardless of their beneficiary's actual age—to use the *Uniform Lifetime Table.*

The *Joint and Last Survivor Table* reflects the life expectancy of two individuals. The ages in the table range from 0 to 120 years, and it shows the likely number of years that at least one of the two individuals will live. Despite listing all combinations of ages up to 120, this table is used in the RMD context for one purpose: to determine the distribution period for an employee who has named the spouse as the sole designated beneficiary—when the spouse is more than 10 years younger than the employee. This allows the employee to calculate the RMD using a longer life expectancy than under the *Uniform Lifetime Table*, resulting in a smaller RMD.

The third life expectancy table, the *Single Life Table,* is required in several situations. Perhaps the most common use is for determining the distribution period that a beneficiary must use when an employee dies. For example, assume that an IRA owner dies this year at age 75 and has named his 70-year-old sister as the sole beneficiary. Next year, his sister will determine her distribution period using the *Single Life Table*. The life expectancy for a (now) 71-year-old is 16.3 years under the current table.

The tables are also used for "substantially equal periodic payments" under IRC Sec. 72(t)(2)(A)(iv). The Internal Revenue Code contains an exception to the 10 percent early distribution penalty tax for certain pre-59½ distributions. Payments must be properly structured using the life expectancy tables contained in the regulations—and they must continue for at least five years and until the recipient reaches age 59½. This payment stream permits access to retirement funds while also preventing excessive fund depletion. The details of setting up such equal periodic payments are found in Revenue Ruling 2002-62, which the IRS expects to update to reflect the changes in the final life expectancy regulations.

The Transition Rule

The one provision that will likely create the most activity—and questions—is the final regulation's "transition rule." The IRS states that this rule is "designed to recognize that the general population has longer life expectancies than the life expectancies set forth in the formerly applicable Treas. Reg. 1.401(a)(9)-9." The transition rule allows a beneficiary who has already locked into a life expectancy for RMD payouts to use a "one-time reset" to take advantage of the longer life expectancies in the new tables. This situation occurs when the employee died before January 1, 2021, and the beneficiary was using the old life expectancy tables to determine the RMD. Starting in 2022, the beneficiary's RMD is based on the new tables, using the *age* for which the life expectancy was originally determined. An example may help.

Example: Frank died at age 80 in 2018. Frank's nonspouse beneficiary, Rose, was 75 in the year he died. In 2019, the distribution period that Rose must use is 12.7 (the single life expectancy of a 76-year-old). For her distribution in 2021, Rose reduces that figure to 10.7 years: one year for 2020 and one year for 2021. Normally, Rose would then reduce her distribution period by one more year for 2022, to 9.7. But the transition rule permits Rose to reset her distribution period based on the new tables. Rose still uses her *age* in the year following Frank's death, but she simply replaces the old life expectancy, 12.7, with the new one, which is 14.1. She then reduces that figure one year for each subsequent distribution year (2020, 2021, and 2022) to arrive at 11.1 instead of 9.7 (under the old tables).

Although this transition rule makes only incremental decreases in the amount that beneficiaries must distribute, this reset provides some relief for those who wish to distribute the smallest amount required in order to preserve assets. On the other hand, redetermining the distribution periods for beneficiaries who had commenced required distributions before 2022 will entail additional effort by financial organizations, plan administrators, and other advisers.

Note: *The proposed regulations seemed to limit the circumstances under which a beneficiary could use the one-time reset. This apparent limitation was likely unintentional. But the final regulations revised the transition rule wording enough to verify a more expansive interpretation of the rule. So irrespective of how a beneficiary came to use the old* Single Life Table*, the new table can now be used. For those required to use "nonrecalculation" (by reducing the life expectancy by one year for each successive distribution year), the starting age remains the same. Spouse beneficiaries, who may use the "recalculation" method, simply start using the new tables in 2022.*

Key Takeaways

The final regulations are nearly identical to the proposed regulations. While these new regulations are straightforward, there are still some important points to remember.

- The new tables apply for distribution calendar years beginning on or after January 1, 2022.
- The transition rule allows certain beneficiaries a one-time reset to use the longer life expectancies.
- The IRS expects to review these tables every 10 years (or when new mortality studies are published).

- The final regulations will require a significant number of individual RMD payout redeterminations.
- Software platform providers and others may face sizeable programming tasks.

Looking Ahead

Fortunately, the IRS heeded commenters' requests and delayed the final regulations' applicability date to 2022. This will allow more time for all affected parties to integrate the new tables into their processes. The IRS will also release guidance regarding SECURE Act provisions, such as the rule that replaces certain beneficiary life expectancy payments with a requirement to deplete beneficiary accounts after 10 years. As guidance is released, rely on Ascensus to monitor developments and to publish helpful analysis.