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# The Basics of Required Minimum Distributions

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## Ensuring that Uncle Sam Gets His Due

The benefits of retirement accounts such as a traditional IRA or a 401(k) are two-fold:

- Tax-deductible contributions allow individuals to reduce the size of their current tax burden while they are saving for retirement – which effectively lets them save more.
- Tax-deferred growth inside these accounts allows funds to accumulate without concern for an annual tax bill on that growth.

### When It's Time to Pay Taxes

Eventually, however, the government must be paid. The tax benefits of these accounts are provided for one purpose: to help individuals save for retirement. Once an individual reaches retirement age, these same rules now dictate that the funds must be used for retirement purposes and the taxes that have been deferred must be paid.

What does this mean? It means that federal income tax law requires that a minimum amount of money, known as a “required minimum distribution,” or RMD, be withdrawn from these accounts each year, starting at a specific age, known as the Required Beginning Date, or RBD.<sup>1</sup> The amount to be distributed is determined by a special calculation that, in essence, takes the total amount in the account and divides it by the number of years the individual is expected to live. When the required minimum distribution amount is received, it is included as taxable income to the individual and Uncle Sam will, finally, get paid. If an account owner does not make distributions that are large enough, or if distributions are not made at all, a penalty tax of 25%<sup>2</sup> of the amount that should have been distributed is generally due.<sup>3</sup> If the taxpayer promptly corrects the error, the penalty tax is reduced to 10%.

But, one bit of good news is that the amount remaining in the account continues to grow tax deferred.

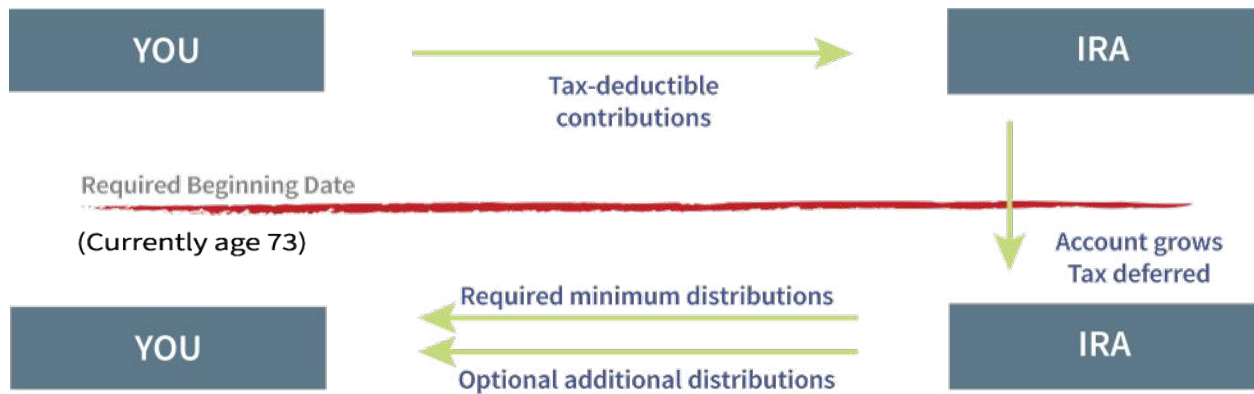
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<sup>1</sup> Under current regulations, the age to begin RMDs increases after 2022 to: (1) age 73 for those born from 1951 to 1959; and (2) to age 75 for those born after 1959. Previously, age 72 was the mandated age to begin RMDs. For non-owner employees, RMDs must begin by April 1 of the year after the *later* of (a) the year an employee reaches the RBD; or (b) the year the employee retires. For more-than 5% owners, RMDs *must begin* by April 1 of the year after the year they reach the RBD.

<sup>2</sup> Applicable to required minimum distributions after December 29, 2022. Under prior law, the penalty tax was 50% of the amount that should have been distributed.

<sup>3</sup> This is federal income tax law. State or local income tax law may differ.

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# Disclosure Notice

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