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By Kathryn J. Kennedy

The SECURE Act, enacted late in December of 2019, made a number of significant changes for qualified retirement plans. This article deals with the changes the Act made that affect the required minimum distribution rules applicable to qualified defined contribution plans.

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to be applicable to IRAs [IRC § 408(a)(6)], Code Section 403(b) annuity plans [IRC § 403(b)(10)], and Code Section 457 eligible deferred compensation plans [IRC § 457(d)(2)]. The required minimum distribution rules also apply to Roth IRAs, but only once the Roth owner dies. [IRC § 408A(c)(4)]

The rules carry with them a heavy 50 percent excise tax applicable to the difference of what was distributed from the plan and what should have been distributed; hence, they have the attention of both plan participants and plan administrators. [IRC § 4974]

This article deals only with the required minimum distribution rules applicable to qualified defined contribution plans and assumes that the plan participant (an employee) is eligible to elect a form of payment that includes installment payouts (e.g., the plan participant can elect to distribute 5 percent of his/her account balance in a given year, in lieu of electing a life annuity form of payment). Such a form of payment affords the most flexibility to a plan participant wishing to defer receipt of monies from his/her account balance.

The SECURE Act, enacted late in December of 2019, made a number of significant changes for qualified retirement plans. One of those changes involved alterations to the required minimum distribution rules. [Further Consolidated Appropriations Act of 2020, Pub. L. 116-94, Div. O, Setting Every Community Up for Retirement Enhancement (SECURE) Act, §§ 114, 401] Congress delayed the age at which the RBD is triggered, which delayed the commencement of the required distributions, but altered the length of payment of benefits to certain named beneficiaries. Hence, what Congress gave with one hand, it taketh away with the other hand. The purpose of this article is to review those changes and highlight areas that are in need of regulatory interpretation.

Terms of the Statute Pre-SECURE and Post-SECURE

As the minimum distribution rules hinge on an employee’s RBD, we will first look to Code Section 401(a)(9)(C).

The statute (prior to SECURE) defines the RBD as the April 1 following the calendar year in which the employee attains age 70½; in the case of an employee who is not a five-percent owner, RBD is defined as the April 1 following the calendar year in which the employee retires if such date is later. (Unfortunately, the Code does not define what is meant by “retirement.”) Thus, for example, an employee who is not a five-percent owner could delay retirement until he or she actually retired at age 74, and then trigger his/her RBD to be the April 1 following the calendar year in which he/she attained age 74. However, the Code and its regulations make it clear that the first year of distribution is the calendar year in which the employee attains age 70½; only payment of that first year’s distribution may be delayed until the following April 1. [IRC §401(a)(9)(C)(i) and Treas. Reg. § 1.401(a)(9)-5, Q&A-1(b)] Thereafter, subsequent required minimum distributions are to be made by December 31 of the given distribution year. [Treas. Reg. § 1.401(a)(9)-5, Q&A-1(c).]

The SECURE Act simply changed the triggering age from age 70½ to age 72, effective for distributions required to be made after December 31, 2019. [SECURE Act § 114]

Code Section 401(a)(9)(A): Lifetime Minimum Distributions

Code Section 401(a)(9) provides rules for distributions during the life of the employee participants under Code Section 401(a)(9)(A) and rules for distributions after the death of the employee under Code Section 401(a)(9)(B). The statute requires that distributions begin as of the employee’s RBD, and once an employee attains his/her RBD, distributions begin, in accordance with IRS regulations, over the life of the employee (or life expectancy) or the joint lives of the employee and a designated beneficiary (or their joint life expectancies).[IRC § 401(a)(9)(A)(i)-(ii)] References to the life of the employee or the joint lives of the employee and his/her beneficiary would assume that a life annuity or joint and survivor life annuity distribution would apply, whereas references to the life expectancy of the employee or the joint life expectancies of the employee and his/her beneficiary would assume that an installment form of distribution would apply. As most employees seeking to use the benefits of the minimum distribution rules would not select an annuity form of payment, the statute recognizes that an installment form of payment is possible.

In non-annuity situations, the Treasury Regulations outline the life expectancies to be used. [Treas. Reg. § 1.401(a)(9)-9.] The tables were recently updated to reflect increased life expectancies, effective for required minimum distributions beginning on or after January 1, 2022. [85 Fed. Reg. 72,472 (Nov. 12, 2020)] Generally, for lifetime distributions, the Uniform
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Lifetime Table is used. [Treas. Reg. § 1.401(a)(9)-5, Q&A-4(a)] However, if the participant’s spouse is the sole beneficiary and he/she is more than 10 years younger than the participant, the Joint and Last Survival Table would be used. [Treas. Reg. §1.401(a)(9)-5, Q&A-4(b)]

Code Section 401(a)(9)(B): Minimum Distributions After the Participant’s Death

The statute sets forth the minimum distribution rules applicable after the death of the employee.

- Under the header “Where Distributions have begun under subparagraph (A)(ii):” If distributions had already begun to the employee (as his/her RBD was triggered), then post-death distributions must be “at least as rapidly” as under the method used by the employee. [IRC § 401(a)(9)(B)(i)] As Code Section 401(a)(9)(A)(ii) prescribes, distributions beginning on the RBD should have been according to the employee’s life annuity (or his/her life expectancy) or the joint life annuity of the employee and his/her beneficiary (or their joint life expectancies). Hence, the statute assumes that post-death distributions to the employee’s beneficiary will take into account the employee’s remaining life expectancy at the time of death.

- Under the header “5-year rule for other cases:” Code Section 401(a)(9)(B)(ii) provides that, if the employee dies before his/her RBD, the employee’s interest is to be distributed within five years after the death of the employee (known as the five-year rule).

- Under the header “Exception to 5-year rule for certain amounts payable over life of beneficiary:” An exception to the five-year rule applies if a designated beneficiary is named. In such case, the employee’s interest may be distributed over the life or life expectancy of that beneficiary, beginning in the calendar year after the employee’s death, using the life expectancies from the Single Life Table (known as the life expectancy rule). [IRC § 401(a)(9)(B)(iii)] By naming a much younger age beneficiary, the employee could “stretch” the distribution stream over long periods of time as the life expectancy rule used the beneficiary’s life expectancy. For example, suppose that Employee A is age 75 in the calendar year of her death, A could have named her son, age 40 (in the following calendar year), as her designated beneficiary, thereby allowing her son to extend the distributions over his life expectancy of 43.6 years!

It was this ability to “stretch” distributions over a long period of time that Congress wanted to prevent under the SECURE Act.

Code Section 401(a)(9)(B)(iv) gives the surviving spouse a delayed commencement date until the date the employee would have attained age 70½ (age 72 under SECURE). It also provides that, if the surviving spouse dies after the employee but before distributions have begun to him/her, the spouse is treated as the employee for purposes of the five-year rule and its exceptions. [IRC § 401(a)(9)(B)(iv)]

Code Section 401(a)(9)(D): Life Expectancies

The statute provides that (except in the case of a life annuity) the life expectancy of the employee and spouse would be redetermined annually. This meant that, if the spouse began to receive distributions following the death of the employee, his/her life expectancy could be redetermined every year (known as the recalculation method). This is preferable, as one’s life expectancy improves as one ages. In contrast, the regulations require beneficiaries (excluding the spouse) to use their life expectancy (determined in the calendar year following the employee’s year of death), reduced by one for each year thereafter (known as the nonrecalculation method).

For example, a beneficiary age 60 in the first year of distribution uses his/her life expectancy of 25.2 under the Single Life Expectancy Table. In the next year, he/she will use a life expectancy of 25.2, minus one, or 24.2; in the next year, 23.2; etc. After 26 years, all funds would have been distributed to the beneficiary. In contrast, if the beneficiary was the spouse age 60 in the first year of distribution, he/she can continue to use his/her actual life expectancy each year until age 111 (when the table assumes the individual is deceased). The spouse’s first year’s divisor is also 25.2, but his/her subsequent divisors are redetermined under the table each year (i.e., the second year distribution uses 24.4 as the divisor, the third year distribution uses 23.5 as the divisor). That prolongs the distribution for 51 years, instead of 26 years, provided the beneficiary is still alive!

Code Section 401(a)(9)(E): Designated Beneficiaries

The statute provides that the term designated beneficiary means an individual designated as a beneficiary
by the employee. [IRC § 401(a)(9)(E)] As an entity such as one’s estate, charity, or trust is not an individual, naming such entities as a beneficiary prevents the use of the life expectancy rules of the statute by the beneficiary.

**Code Section 401(a)(9)(F): Minor Children as Beneficiary**

The statute provides that payments that are made to the employee’s child until such child reaches the age of majority (or dies, if earlier), may be treated, for purposes of the distribution rules, as if such payments were made to the surviving spouse, to the extent they are payable to such spouse upon cessation of the payments to the child. This rule applies in the context of defined benefit plans and annuity contracts. While the term “majority” is not defined in the statute, the attendant regulations provide that a child may be treated as having not reached the age of majority if he/she has not completed a “specified course of education” and is under the age of 26. [See Treas. Reg. §1.401(a)(9)-6, Q&A-15, published in 69 Fed. Reg. 33,288 (June 15, 2004)]

The SECURE Act altered the minimum distribution rules in the context of designated beneficiaries who do not satisfy the new definition of an “eligible designated beneficiary.” [SECURE Act, § 401(a)(2), amending IRC § 401(a)(9)(E)(ii)] Before discussing these changes, a description of the IRS’ proposed 2001 regulations and its 2002 final regulations is necessary. The original 1987 regulations regarding minimum distributions were exceedingly complex and required certain election requirements. [Prop. Reg. § 1.401(a)(9)-1, published in 52 Fed. Reg. 28,070 (July 27, 1987), supplemented in 62 Fed. Reg. 67,780 (Dec. 30, 1997)] In an effort to make the rules easier for both plan participants and plan administrators, the 2001 proposed regulations made a number of simplifications applicable not only during the employee’s lifetime while receiving the minimum required distributions, but also for the beneficiaries, for distributions post-death of the employee. [Prop. Reg. §§ 1.401(a)(9)-0 through -8, published in 66 Fed. Reg. 3,928 (Jan. 17, 2001)] Four simplification rules were set forth in the 2001 proposed regulations:

1. Adopt a simple, uniform table that all employees can use in determining the required minimum distribution. Such table use the employee’s age in the year of distribution and an assumed beneficiary deemed to be 10 years younger than the employee. [See Preamble to the Proposed Regs, id. (Preamble)] For example, at age 71, the uniform table permitted a divisor of 26.5 to be used (which was the employee’s age 71 and his/her presumed beneficiary age 61);

2. Permit the required minimum distribution during the employee’s lifetime to be recalculated under the uniform table and to be determined without regard to the actual beneficiary’s age (unless the spouse was the named beneficiary and more than 10 years younger than the employee). [Id.] Thus, the named beneficiary was the spouse age 50, with an employee age 71 in the year of distribution, the actual joint life expectancy of 35.0 years could be used, in lieu of 26.5;

3. Permit the beneficiary to be determined as late as the end of the calendar year following the employee’s year of death. [Id.] The final regulations changed this date to the September 30 of the calendar year following the employee’s year of death. [Treas. Reg. § 1.401(a)(9)-4, Q&A-4] This allowed the employee to change the designated beneficiary after the RBD without increasing the required minimum distribution and allowed the beneficiary to be changed after the employee’s death (e.g., one of the beneficiaries could disclaim his/her rights or could be cashed out); and

4. Permit the calculation of post-death minimum distributions to take into account an employee’s remaining life expectancy at the time of death, allowing distributions in all cases to be spread over a number of years after death. [See Preamble, supra] This goal was consistent with the terms of the statute under Code Section 401(a)(9)(A)(ii) that, once benefits had commenced to the employee as of his/her RBD, distributions upon death would be “at least as rapidly” and distribution over the employee’s life expectancy was included within that dictate.

The 2002 final regulations incorporated all of these goals. It resulted in a set of rules that are best understood if the employee dies before his/her RBD versus survives to RBD and dies on or after his/her RBD.

- If the employee dies before his/her RBD and has a designated beneficiary, the life expectancy rule in Code Section 401(a)(9)(B)(iii) prevails, instead of the five-year rule, permitting distributions to “stretch” over the beneficiary’s single life expectancy. In the case where a designated beneficiary is
not named (e.g., the estate, trust, or charity), the five-year rule prevails. [Treas. Reg. § 1.401(a)(9)-3, Q&A-1]

- If the employee survives to his/her RBD, the annual minimum distributions are determined in accordance with the uniform table (which assumes the employee has attained a given age and that his/her presumed beneficiary is 10 years younger), each year, as the employee ages. [Treas. Reg. § 1.401(a)(9)-5, Q&A-4(a)] For example, if the employee is age 72 in the year of distribution, the uniform table factor to be used is 25.6; a year later, when the employee attains age 73, the uniform table factor changes to 24.7. Note the actual joint life expectancy tables are used if the spouse is the sole beneficiary and the age difference is greater than 10 years. [Treas. Reg. § 1.401(a)(9)-5, Q&A-4(b)] The regulations go on to describe how minimum distributions are required once the employee dies. The required minimum distribution in the year of death is computed the same as if the employee were alive. [Treas. Reg. § 1.401(a)(9)-5, Q&A-4(a)] Thereafter, consistent with the goal of the regulations to take into account the employee’s remaining life expectancy upon death, the regulations set forth the rules as follows:

— If the employee does not have a designated beneficiary, the remaining life expectancy of the employee (reduced by one, for each year thereafter) is to be used;
— If the employee does have a designated beneficiary, the distribution period is the longer of the employee’s remaining life expectancy (reduced by one, for each year thereafter) or the beneficiary’s remaining life expectancy (reduced by one, for each year thereafter). [Treas. Reg. § 1.401(a)(9)-5, Q&A-5(a)] Special rules existed if the spouse was the named designated beneficiary, such that he/she can recalculate his/her life expectancy. [Treas. Reg. § 1.401(a)(9)-5, Q&A-5(c)(2)]

SECURE Act Changes

With this background, we can now layer on the changes made by the SECURE Act to discover how the minimum distribution rules have changed. The legislative history makes it clear that Congress wanted, in the defined contribution plan context, to expand the five-year rule to a ten-year rule, and to apply such rule for distributions to designated beneficiaries after the employee’s death, regardless of whether the employee dies before, on, or after his/her RBD. [See Setting Every Community Up for Retirement Enhancement Act of 2019, Ways and Means Rept., H.R. Rep. No. 116-65 Part 1, at 108, available at HR065P1.PS (congress.gov). See also Staff of the Joint Comm. on Tax’n, Description of H.R. 1994, The “Setting Every Community Up for Retirement Enhancement (SECURE) Act of 2019,” 116th Cong. 1st Session (2019), at 74-75 available at x-11-19-5178.pdf]

Hence, distributions to named beneficiaries would have a maximum distribution period of 10 years. However, Congress intended to preserve the existing life expectancy rule for certain beneficiaries, namely, those that meet the definition of “eligible designated beneficiaries.” [SECURE Act § 401(a)(1), adding IRC § 401(a)(9)(H)(iii)] This new term of art would cover a surviving spouse; minor children of the employee until the age of majority; a disabled beneficiary; a chronically ill beneficiary; and a designated beneficiary not more than 10 years younger than the employee. [SECURE Act § 401(a)(2), amending IRC § 401(a)(9)(E)(ii)(I)-(V)] As an aside, the term “majority” for purposes of a minor child is not defined by the legislation, resulting in a serious flaw within the statute. Under state law, majority age can range from ages 18, 21, or 23 [See Elissa Shu, “The age of majority (and the UTMA account distribution age) in every state,” Policygenius, Dec. 20, 2020, available at Age of Majority by State as of 2021 (policygenius.com)], whereas majority age can range from ages 19, 24, or 26 under various federal laws. [See IRC § 152(a)(1), which defines a “qualified child” for purposes of a taxpayer’s deduction for personal exemption as a child who has not yet attained age 19 or, in the case of a student, who has not yet attained age 24. See also, the Patient Protection and Affordable Care Act (PPACA) was originally enacted on March 23, 2010 as Pub. L. No. 111-148, as modified by the Health Care and Education Reconciliation Act of 2010 (HCRA) on March 30, 2010 as Pub. L. No. 111-152, and referred to as the Affordable Care Act (ACA), §1001 (adding PHSA §2714; HCRA §2301), which defines a child as one who has not yet attained age 26] The IRS will have to provide guidance on this issue and hopefully will utilize a federal definition of the term.

Given the intent of the legislative history to eliminate stretch distributions except for a select class of beneficiaries, one would have expected Congress to have amended both the distribution rules of Code
Section 401(a)(9)(B)(i) (i.e., post-death distribution rules applicable after the employee attains on or after his/her RBD) and the distribution rules of Code Sections 401(a)(9)(B)(ii) and (iii) (i.e., post-death distribution rules applicable when the employee dies before his/her RBD). However, Congress only amended the distribution rules of Code Sections 401(a)(9)(B)(ii) and (iii), which makes interpreting the changes problematic.

The legislative changes made by the SECURE Act add a new subparagraph (H) to Code Section 401(a)(9), which provide new distribution rules for certain defined contribution plans. [SECURE Act, § 401(a)(1)] It also amends Code Section 401(a)(9)(E), by adding a new definition as to who is an eligible designated beneficiary. [SECURE Act, § 401(a)(2)] The effective date of these changes applies to distributions for employees who die after December 31, 2019. [SECURE Act, § 401(a)(3)(A)]

- The existing five-year rule under Code Section 401(a)(9)(B)(ii) (which is used if the employee dies before his/her RBD) continues to apply if there is no designated beneficiary (e.g., the estate, a charity, or trust is named). This leaves open the question as to what rule applies if the employee dies on or after his/her RBD and has no designated beneficiary. Will the rule under the existing regulations prevail?
- If a designated beneficiary is named, Code Section 401(a)(9)(B)(ii) is modified to substitute 10 years for five years (hence, a new 10-year rule), which is to be applied whether or not distributions of the employee’s interest have begun in accordance with Code Section 401(a)(9)(A) (meaning whether or not the employee attains his/her RBD). Does this change result in a modification of the post-death distribution rules under Code Sections 401(a)(9)(B)(i) and (ii) and (iii), even though only the latter provision was altered?
- The statute then amends Code Section 401(a)(9)(B)(iii) (the exception to the five-year rule for certain amounts over the life of beneficiary) to make it apply only in the case of an eligible designated beneficiary (a new term of art). This would appear to create an exception to the five-year rule (which applies if the employee dies before to his/her RBD) for eligible designated beneficiaries. However, the legislative history indicates that the new ten-year rule (which should apply whether the employee dies before his/her RBD or on or after his/her RBD) should have an exception for eligible designated beneficiaries. The IRS will need to provide guidance in this area. Does it matter whether the exception for eligible designated beneficiaries applies under the five-year rule versus the new ten-year rule? Yes, because if the exception for eligible designated beneficiaries applies to the five-year rule, that would leave intact the final regulation rules extending such beneficiaries the longer of the employee’s remaining life expectancy or the beneficiary’s remaining life expectancy, when the employee dies on or after his/her RBD.

- Neither the new terms of the statute nor its legislative history indicates whether and how Congress intended to change the 2002 final regulations in the context of post-death distributions once an employee attains his/her RBD and then dies. Remember under the final regulations, if the employee attains his/her RBD and then dies, distributions under all cases were to be spread over a number of years after the employee’s death, providing at minimum the employee’s remaining life expectancy. [See Preamble, supra] Will the IRS permit distributions to an ineligible designated beneficiary upon the death of the employee after his/her RBD to commence over the longer of the beneficiary’s life expectancy or the ten-year limit?

What's the IRS Thinking?

While the IRS has yet to issued proposed regulations reflecting the SECURE Act changes, we have a glimpse of the IRS’s thinking in its recent Publication 590-B for 2020 returns. [See IRS, Distributions from Individual Retirement Arrangements (IRAs): For use in preparing 2020 Returns, Publication 590-B (Mar. 25, 2021), available at https://www.irs.gov/publications/p590b] As one would expect, the IRS reviews the minimum distribution rules in the context of an IRA owner dying before his/her RBD versus dying on or after his/her RBD.

In the context of the IRA owner dying before his/her RBD, the Publication states the following:

- It confirms the use of the five-year rule if no individual designated beneficiary has been named. It reiterates that the five-year rule does not require annual distributions; simply that the distribution of the IRA owner’s entire account be distributed by December 31 of the year containing
the fifth anniversary of the owner’s death. [Id. at p. 11, under the headers of the “5-year rule” and “Beneficiary not an individual”]

• It confirms that an eligible designated beneficiary may elect the life expectancy rule (i.e., distributions over his/her life expectancy), unless he/she elects to take distributions using the five-year rule or the ten-year rule, whichever rule is applicable. [Id., under the header of “Individual designated beneficiaries”] But the Publication goes on to say that the eligible designated beneficiary could only elect the ten-year rule if the owner died before reaching his/her RBD. [Id., under the header of the “10-year rule”] That appears to be inconsistent with the statutory changes that the new ten-year rule applies “whether or not distributions of the employee’s interests have begun in accordance with subparagraph (A).”

• It then suggests that a designated beneficiary who is not an eligible designated beneficiary must take minimum distributions using his/her life expectancy. In its first example on page 12 of the Publication, there is an adult child named as designated beneficiary of his father’s IRA, where the father dies during 2020. The adult child is age 53 in 2021. The Publication states that the adult child should use the Single Life Expectancy Table in 2021, which produces a divisor of 31.4, and should receive a minimum distribution for 2021 of $3,185 ($100,000, the account balance, ÷ 31.4). [Id. at p. 12, under the first header entitled “Example”] Such interpretation would clearly contradict the terms of the statute and its legislative history which would have required that the ineligible designated beneficiary receive distributions under the ten-year rule, which, if applied consistent with the five-year rule, would not require annual distributions, but simply that distribution be made in full by the end of the calendar year containing the tenth anniversary of the IRA owner’s death. Shortly after its publication, the IRS announced that the 2020 Publication 590-B would be revised in order to clarify its description of the ten-year rule. [See Revisions to the 2020 Publication 590-B, available at Revisions to the 2020 Publication 590-B | Internal Revenue Service (irs.gov), dated May 13, 2021] In the announcement, the IRS sets forth another example in which the IRA owner dies in 2020 at age 74 and names his brother (age 65 in 2021) as beneficiary. [Id.] As the brother is less than 10 years younger than the IRA owner, he is an eligible designated beneficiary and thus, is eligible to use Table I to produce a life expectancy of 21.0 in 2021, for purposes of computing his required minimum distribution. [Id.] Elsewhere in the original 2020 Publication 590-B, the IRS does describe the ten-year rule, similar to the five-year rule, as requiring full distribution by December 31 of the year containing the tenth anniversary of the owner’s death. [See IRS Publication 590-b, at p. 11] In the announcement, the IRS did not provide an example of a distribution to an individual who is not an eligible designated beneficiary, after the IRA owner dies.

In the context of the IRA owner dying on or after his/her RBD, the Publication states the following:

• If a designated beneficiary has not been named, the Publication retains the existing rule under the regulations to allow for distributions over the employee’s remaining life expectancy, reduced by one year for each year thereafter; [Id. at p. 12, under the second header labeled “Example”]

• If the beneficiary is an eligible designated beneficiary, the Publication retains the existing rule under the regulations to allow for distributions over the longer of: (1) the beneficiary’s single life expectancy determined in the year following the employee’s death, reduced by one for each year thereafter, or (2) the employee’s life expectancy in the year of death, reduced by one for each year thereafter. [Id. at p. 10, under the header “Owner Died On or After Required Beginning Date”] If the sole beneficiary is the surviving spouse, the spouse may recalculate his/her life expectancy each year thereafter. [Id., under the header “Surviving spouse is sole designated beneficiary”]

• If an individual is named as the designated beneficiary but does not meet the definition as an eligible designated beneficiary, the Publication requires the entire account balance to be fully distributed within 10 years after the owner’s death, thereby eliminating the use of the employee’s remaining life expectancy in determining the distribution period. [Id., under the header “Designated beneficiary who is not an eligible designated beneficiary”] Most practitioners will find this interpretation awkward as not naming a designated beneficiary may result in a longer distribution period, i.e., the employee’s remaining life expectancy.
Conclusion

The purpose of this article was to highlight the changes made by the SECURE Act regarding the required minimum distribution rules and to note areas in which IRS guidance is needed. As Congress suspended the minimum distribution rules for 2020 due to the pandemic, [Pub. L. No. 116-1367, The Coronavirus Air, Relief, and Economic Security Act of 2020 (CARES), § 2203, relaxed the minimum distribution rules for 2020 for defined contribution plans and IRAs] immediate guidance for 2020 has not been necessary. However, as we move into 2021, guidance is going to be needed in assisting employees and IRA owners in their determination of the required minimum distribution rules from defined contribution plans and IRAs.