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The TCJA raised the federal estate tax exemption to over $11 million per decedent, which means that relatively few clients will be exposed to this tax. Many advisors, therefore, are placing more emphasis on income tax issues that heirs will face.

Seymour Goldberg, senior partner at Goldberg & Goldberg, a law firm in Melville, NY, says one area of possible concern is taking the required minimum distribution (RMD) for the year of death.

"Recently," he says, "I’ve become aware of a number of cases where this RMD wasn’t taken on time, and penalties could be significant."

Let’s suppose Joe dies on October 15, 2019, with an IRA valued at $1 million on December 31, 2018. "In most cases, he would not have taken his RMD, because IRA owners often maximize potential tax-deferred growth by waiting until late in the year to take their RMD, or else they receive RMD payments in monthly installments," says Goldberg, whose newly released book, Effective Use Of IRA Assets In Estate Planning (includes IRS compliance issues and asset protection planning), is available at: trustestateprobate.com/publications-for-purchase-2018-2019/.

Joe would have been age 75 in 2019, his year of death. Thus, his life expectancy under the IRS Uniform Lifetime Table would have been 22.9 years. Dividing $1 million (year-end 2018 IRA balance) by 22.9 (life expectancy for year of death) equals $43,668, which would have been Joe’s 2019 RMD.

Before he died, assume Joe had taken only one IRA distribution in 2019 for $10,000. The unpaid RMD balance of $33,668 would be payable to Joe’s IRA beneficiary. Failure to timely pay this amount to Joe’s beneficiary could generate a 50% penalty ($16,834) to Joe’s beneficiary for the RMD shortfall.

According to Goldberg, this unpaid RMD for the deceased IRA owner’s year of death should be paid to the beneficiary as soon as possible. The official deadline for this distribution is December 31 of the year of death, but that may not be possible.

If Joe had died on October 15, as stated, it may take longer than 2½ months to discover the shortfall and distribute the RMD balance. This is a real-world IRS significant noncompliance issue that may affect many people.

“Advisors who represent IRA beneficiaries should urge them to pay any RMD shortfall for the year of death, as soon as possible,” says Goldberg. "If the deadline was missed, the beneficiary should file IRS Form 5329, indicating the shortfall and requesting a waiver of the 50% penalty."

Let’s continue our example as if we are now in the year 2020. Assume that Joe’s widow, Kat, was the sole IRA beneficiary. Kat did not take out the unpaid distribution before December 31, 2019.

On the Form 5329 waiver request – filed shortly after Kat found out about the unpaid distribution in June 2020 – Kat should explain that Joe died on October 15, 2019, and she then withdrew the RMD shortfall of $33,668 as soon as she became aware of it. “Kat also should include information about when she became aware of the shortfall, who brought it to her attention, and that she will report the $33,668 as taxable income for 2020 – the calendar year that she discovered the RMD shortfall and received the payout,” says Goldberg.

As the surviving spouse, Kat cannot roll over the unpaid RMD of $33,668. “According to IRS rules, an RMD is not eligible for a rollover,” says Goldberg. "In addition, the first monies taken out during a given year from the traditional IRA are considered to be applied toward the RMD amount for that year.”
Seymour Goldberg, CPA, MBA, JD is the senior partner in the law firm of Goldberg & Goldberg, P.C. in Long Island, New York. Mr. Goldberg was formerly associated with the Internal Revenue Service (IRS). He conducted many continuing education programs with the IRS and other organizations on the retirement distribution rules. He has written several books on IRA issues for the American Bar Association, which can be found in law school libraries throughout the United States. They are Inherited IRAs, What Every Practitioner Must Know, 2017 Edition and IRA Guide to IRS Compliance Issues, Including IRA Trust Violations, and his newly released book Effective Use Of IRA Assets In Estate Planning (includes IRS compliance issues and asset protection planning), available at trustestateprobate.com/publications-for-purchase-2018-2019.

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