



Retirement Planning Software, Inc
RetirementWorks®

72(t) Distributions

The 72(t) Distributions module calculates the maximum amounts that plan participants may withdraw from a tax-qualified plan if they begin withdrawals before they have attained the age of 59½ ("72(q)" for non-qualified annuities).

Please note that the input screens and on-line Help for the 72(t) Distributions calculator and the Required Minimum Distribution calculator are nearly identical. Certain fields that pertain only to Required Minimum Distribution calculations will remain suppressed if they are not needed to perform a 72(t)/72(q) calculation. We have noted those fields below.

The screenshot shows the RetirementWorks 72(t) Distributions input screen. The window title is "RetirementWorks®" and the menu bar includes "File", "Print", "Calculations", "Windows", and "Help". The main window title is "72(t) Distributions".

Plan basics

Name: Date of birth:

Type of plan:

Plan balance

Adjusted year-end balance: \$ Calendar year this balance applied (yyyy):

For 403(b), amount of this balance that is "grandfathered" (i.e., 12/31/86 balance): \$

Single or Joint life

Should calculations be based on single or joint life expectancy? Single Joint

Who is the beneficiary? Spouse only Non-spouse only Spouse plus non-spouse

Spouse date of birth: Date of birth of oldest non-spouse beneficiary:

Withdrawal dates and options

If plan owner has died, year of death: If spouse has died, year of death:

Did regular distributions start in a previous year? Yes No

Year withdrawals started (yyyy): Option elected:

Option to be illustrated:

Retirement year: 5% Owner: Yes No Gov't or church employee: Yes No

Initial withdrawal date:

Interest rate to be used in 72(t) calculations:

Press <F1> for Help at any time

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When to Use This Calculator

72(t) calculations help IRA owners and participants in Defined Contribution plans obtain money from their plans without paying penalty taxes. Typically in such plans, withdrawals made before age 59½ are subject to a 10% tax penalty, unless certain circumstances (such as death or disability) apply. For most people, the easiest way to avoid the penalty is to take “substantially equal periodic payments” as authorized by Internal Revenue Code §72(t). IRS regulations define various methods of calculating such payments, which have therefore come to be known as 72(t) calculations (or 72(q) for non-qualified annuities).

In most cases, the 72(t) calculation is, at most, a once-in-a-lifetime calculation, and the same result is simply carried forward into future years (for five years or to age 59½, whichever is later). Required Minimum Distribution (RMD) calculations may be used as an acceptable 72(t)/72(q) method, and these would require new calculations every year – except that these methods generally result in much lower numbers, and therefore are rarely used. Usually the goal of a client who needs a 72(t) calc is to take as much as possible, not as little as possible.

Starting in October of 2002, the IRS has authorized a one-time change in method. If either the amortization or the annuitization method has been in use, a taxpayer can make a one-time switch to the RMD method in order to reduce the payment amount. The purpose is to enable people whose accounts have been depleted by adverse investment experience to reduce their withdrawals in order to help stem the reduction in the account balance. However, the IRS does not restrict the change in method to cases where there has been adverse experience. The change in method may only be *to*, not *from*, the RMD method, and may not be *to* either of the other methods.

Most financial companies consider 72(t)/72(q) calculations to be an important service to clients, but not a particularly pleasing one. Such companies naturally like to conserve assets in their products, while the purpose of the calculation is to show the highest possible amount that the client may withdraw without penalty. Nonetheless, tax law compliance is in everyone’s interest, and for this reason many financial companies and individual representatives consider it important to provide this calculation where it is appropriate.

Please note that 72(t) rules do not apply to Section 457 plans or Roth IRAs.



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How to Use This Calculator

The input screen is divided into four sections. Start at the top of the input screen and work your way down. As you do so, certain fields and certain options will be enabled or disabled, according to what choices you make above. This will guide you in your inputs. Use the detailed instructions that follow, or press the <F1> key at any time during the input process to obtain on-line Help.

To compare the various options available, you may select the "Compare alternative methods" option in the bottom section of the input screen, under "Option to be illustrated." This selection will produce a report in which all available calculation methods and their results are listed on one page. To obtain a detailed explanation of how each method was calculated, however, you will need to select each option individually and run separate reports for them.

When you have finished entering all the required information, use the "Print" menu to print or preview the results.



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Detailed Input Instructions

Name

Enter the fund owner or plan participant's name, as it should appear on the printed report.

Date of birth

Enter the fund owner's date of birth in mm/dd/yyyy format. This information is always required.

Type of plan

Select the type of plan from the pull-down list. It is important to indicate the correct plan type since different plans follow somewhat different rules under IRS regulations. All applicable plans fall into one of four categories:

- **401(k) / 401(a) / Misc. def. contr.** This category includes any plans not listed in either of the other categories below. Please note that 72(t) rules do not apply to Section 457 plans.
- **403(b)** This category includes only 403(b) plans (also known as tax-sheltered annuities or tax-deferred annuities, whether they are actually funded with annuities, mutual funds, or other financial products).
- **IRA / Simple IRA / SEP IRA** This category covers any kind of IRA plan subject to the rules in question. Note, however, that Roth IRA plans are NOT subject to these rules.
- **Non-qualified** This option is available for 72(q) calculations

Defined Benefit plans, non-qualified retirement plans (including Section 457 plans), and Roth IRAs are not subject to the distribution rules that apply to 401(k) plans, IRAs, 403(b) plans and the other plans listed above. Do not use this software for those plans.



Adjusted year-end balance

For 72(t) or 72(q) distributions using the Required Minimum Distribution (RMD) formula: Enter the total adjusted balance as of December 31 of the applicable year (see below). For 72(t) and 72(q) calculations that use the RMD formula, it may be permissible, or even preferable, to use the balance as of the date of the first withdrawal, if the first year's withdrawal is the one being calculated (the regulations are not specific about this matter).

For 72(t) or 72(q) distributions using amortization or an annuity factor: Enter the total balance as of the date the first distribution is being made, which is normally sometime during the current year.

For 72(t) or 72(q) calculations that use the RMD formula, you may instead use the average value from the end of the previous year to the date of the withdrawal, if you wish, or any other balance that is "determined in a reasonable manner based on the facts and circumstances" (see IRS Rev. Ruling 2002-62).

For 72(q) calculations (non-qualified annuities only), use the total balance as of the distribution date.

For a 403(b) plan, this balance includes any grandfathered amounts (i.e., plan balances accrued as of December 31, 1986).

Calendar year this balance applied (yyyy)

Since the IRS now allows some flexibility in determining what plan balance is being used, the year for the plan balance could vary, and is therefore not determinative of anything. Therefore it is no longer a useful input for these calculations, and this field is now disabled for 72(t) or 72(q) calculations.

For 403(b), amount of this balance that is "grandfathered" (i.e. 12/31/1986 balance)

This field is only available in the Required Minimum Distributions calculator, and is always suppressed on the 72(t) Distributions calculator window. Grandfathered amounts are not used in 72(t) calculations because the applicable divisors (from the IRS Minimum Distribution Incidental Benefit table) are not defined prior to age 70½.



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Should calculations be based on single or joint life expectancy?

72(t) and 72(q) distribution calculations are generally based on some measure of life expectancy.

If there is no beneficiary for the account, or if any beneficiary is not a person (e.g. the fund owner's estate, a trust that does not meet specific requirements outlined in IRS Proposed Reg. 1-401(a)(9), a corporation, or another non-personal entity), select "Single".

If there are one or more personal beneficiaries named for the fund, and if there are no non-personal beneficiaries, then you can select "Single" or "Joint". Single life expectancy is more advantageous if you want to maximize annual withdrawals.

Who is the beneficiary?

This field is activated if you have chosen "Joint" in the "Should calculations be based on single or joint life expectancy?" field above.

Select the appropriate beneficiary. This choice is based only on the principal beneficiary(ies), not on any contingent beneficiaries. For example, if the spouse is the principal beneficiary, and the children are to be beneficiaries only if the spouse dies before the fund owner dies, then the children are merely contingent beneficiaries, and the correct selection is "Spouse only". If, however, the fund is to be split between the spouse and the children when the fund owner dies, then select "Spouse plus non-spouse".

In general, the correct beneficiary designation is the one in effect at the time that distributions begin. If the beneficiary is subsequently changed, you should use the new beneficiary designation in this field ONLY if the new designation is less advantageous than the old. That is, you may not change from non-personal to personal beneficiaries, from single to joint, or from non-spouse (or spouse plus non-spouse) to spouse only. Or, to be more precise, although the actual beneficiaries may be changed, the calculations must be done as if the beneficiary had not changed. However, if you change from a more favorable to a less favorable beneficiary designation (personal to non-personal, joint to single, spouse to non-spouse), then the newer, less advantageous designation must be entered.

Spouse date of birth

This field will become active if you've chosen "Joint" in the "Should calculations be based on single or joint life expectancy?" field and you have selected either "Spouse only" or "Spouse plus non-spouse" in the "Who is the beneficiary?" field.



Enter the spouse's date of birth in mm/dd/yyyy format.

Date of birth of oldest non-spouse beneficiary

This field will become active if you've chosen "Joint" in the "Should calculations be based on single or joint life expectancy?" field and you have selected either "Non-spouse only" or "Spouse plus non-spouse" in the "Who is the beneficiary?" field.

Enter the birth date of the oldest non-spouse beneficiary in mm/dd/yyyy format.

Did regular distributions start in a previous year?

If the year being calculated is the first year of 72(t) or 72(q) distribution, click "No". If the calculation is for a withdrawal after withdrawals have already started, click "Yes".

Year withdrawals started (yyyy)

This field becomes active if you've chosen "Yes" in the "Did regular distributions start in a previous year?" field.

For 72(t) and 72(q) calculations, this field is not needed, unless withdrawals are following Required Minimum Distribution (RMD) rules, in which case the year withdrawals started is the year the fund owner first became subject to minimum distributions. For most people this is the year they turned 70½ or the year they retired and is not the year the first withdrawal was actually made.

Option elected

If you selected "Yes" in the "Did regular distributions start in a previous year?" field, this field becomes active. If distributions have already begun, you must indicate which option was originally selected. The options available are the same as the ones described in the following section, except that there is no Comparison option (because after the first distribution, it is not permissible to change the option being used).



Option to be illustrated

If you selected "No" in the "Did regular distributions start in a previous year?" field, this field becomes active. If distributions have not yet begun, select the option to be used. Select from the following options:

- **Distributions using the Required Minimum Distribution rules.** The RMD method is usually much less advantageous for 72(t) or 72(q) calculations, if you are trying to get the maximum amount. However, if you are switching from another method in order to minimize withdrawals that have already started, the RMD method can be advantageous, all the more so since rules and mortality tables that were revamped in 2001 and 2002 further reduce the RMD amounts from what they used to be.
- **72(t) using amortization.** This method amortizes the fund over life expectancy based on a mortality table selected by the IRS, but using an interest rate selected by the fund owner or by the company managing the funds.
- **72(t) using annuity factor.** This method pays out the fund balance using a factor determined by a mortality table and an interest rate selected by the fund owner or by the company managing the funds.
- **Compare alternative methods.** The system will evaluate all available options at once and provide summary results on a single page.

It is worth remembering that, in addition to the above options, distributions may also be paid out by converting the fund to an annuity. Single or joint annuities may be used, as appropriate. If an annuity is used, distributions are those defined in the annuity product, and no separate calculations need to be performed.

If plan owner has died, year of death

This field is available except for 72(t) and 72(q) calculations based on amortization or an annuity factor.

If the fund owner has died, enter the year of death in yyyy format.

If spouse has died, year of death

This field is available when joint life expectancy is used and the spouse is a beneficiary, except



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for 72(t) and 72(q) calculations based on amortization or an annuity factor.

If the spouse has died, enter the year of death in yyyy format.

Retirement year

This field is not needed for 72(t) calculations and remains suppressed.

5% Owner

This field is not needed for 72(t) calculations and remains suppressed.

Gov't or church employee

This field is not needed for 72(t) calculations and remains suppressed.

Initial withdrawal date

Enter the date you expect the first withdrawal to be made in mm/dd/yyyy format. If the first withdrawal has already been made, enter the date it actually occurred.

Interest rate to be used in 72(t) calculations

Enter a "reasonable rate of interest" to be used in calculating amortization and/or annuity factors.

In Revenue Ruling 2002-61, the IRS defined the maximum permissible rate to be "120 percent of the federal mid-term rate...for either of the two months preceding the month in which the distribution begins." The IRS updates these rates monthly, and they appear on its web site at <http://www.irs.gov/taxpros/lists/0,,id=98042,00.html>. This rule is mandatory starting January 2003.