TAX & WEALTH ADVISOR ALERT: NOT FEELING SO SECURE PART II: HOW THE NEW SECURE ACT MAY AFFECT YOUR RETIREMENT AND YOUR TAX SITUATION

The “Setting Every Community Up for Retirement Enhancement” Act (the SECURE Act), signed into law by President Trump on December 20, 2019, pointedly changes many requirements for employer-provided retirement plans, IRAs, and other tax-favored savings accounts. While some of the provisions of the SECURE Act may provide taxpayers with great tax savings opportunities, not all of the changes are helpful, and there may be steps taxpayers can take to minimize its impact. Below is a summary of the key provisions of the SECURE Act that taxpayers should be aware of now, especially since many of the provisions go into effect in 2020.

Repeal of the maximum age for traditional IRA contributions

Before 2020, individuals were prohibited from making traditional IRA contributions upon reaching the age of 70 ½. However, starting in 2020, the SECURE Act allows an individual of any age to make contributions to a traditional IRA if the individual has compensation, such as earned income from wages or self-employment.

This SECURE Act provision eliminates the age limitation, which previously prevented taxpayers older than 72 ½ from contributing to their IRAs. This will allow individuals working into their later years to increase, or catch up with, their retirement savings goals.

Required minimum distribution age raised from 70½ to 72

Pre-2020 retirement plan participants and IRA owners were typically forced to begin taking required minimum distributions, or “RMDs,” from their plan when they reached age 70½. The age 70½ requirement was first established in the early 1960s and, until the SECURE Act, had not been adjusted to account for increases in life expectancy.

Under the SECURE Act, the age at which individuals must begin taking distributions from their retirement plan or IRA is increased from 70½ to 72. Notably, RMDs for individuals who turned 70½ in 2019 are not delayed, and instead, such individuals must continue to take their RMDs under the same rules prior to passage of the SECURE Act.

Increasing the age at which distributions are required allows additional time for the IRA to grow untouched. With many taxpayers remaining in the workforce longer, this provision might prove especially beneficial.

Partial elimination of stretch IRAs

If plan participants or IRA owners died before 2020, beneficiaries (both spousal and nonspousal) were generally allowed to draw from the account and pay taxes on their withdrawals over the beneficiary's life or life expectancy (in the IRA context, this is sometimes referred to as a 'stretch IRA').

However, under the SECURE Act, if a plan participant or IRA owner dies in 2020 or after, distributions to most ***nonspouse beneficiaries*** are generally required to be distributed within 10 years after the plan participant's or IRA owner's death. So, for those beneficiaries, the "stretching" strategy is no longer allowed.

Exceptions to the 10-year rule are allowed for distributions to beneficiaries who are (1) the surviving spouse of the plan participant or IRA owner; (2) a child of the plan participant or IRA owner who has not reached the age of majority; (3) a chronically ill individual; or (4) any other individual who is not more than 10 years younger than the plan participant or IRA owner. Beneficiaries who qualify under this exception may generally still take their distributions over their life expectancy (as allowed under the rules in effect for deaths occurring before 2020).

Overall, this change will cause much larger distributions during peak earning years, which will have a significant impact on the tax obligation of nonspouse beneficiaries. Many retirement and estate plans were created to benefit from the pre-SECURE Act "stretch" tax deferral, so the SECURE Act's elimination of the "stretch IRA" might change how you plan to pass on accumulated accounts, or could influence how you need to handle accounts that are passed down to you. For more discussion on this potential tax impact, see Tax & Wealth Advisor Alert: Not Feeling so SECURE: Proposed Law Could be Costly for Non-Spouse IRA Beneficiaries.

If you are interested in learning more about the SECURE Act and how it might affect your retirement and estate planning goals, please contact attorney Britany E. Morrison at O'Neil, Cannon, Hollman, DeJong & Laing S.C. to discuss how we are able to assist you.