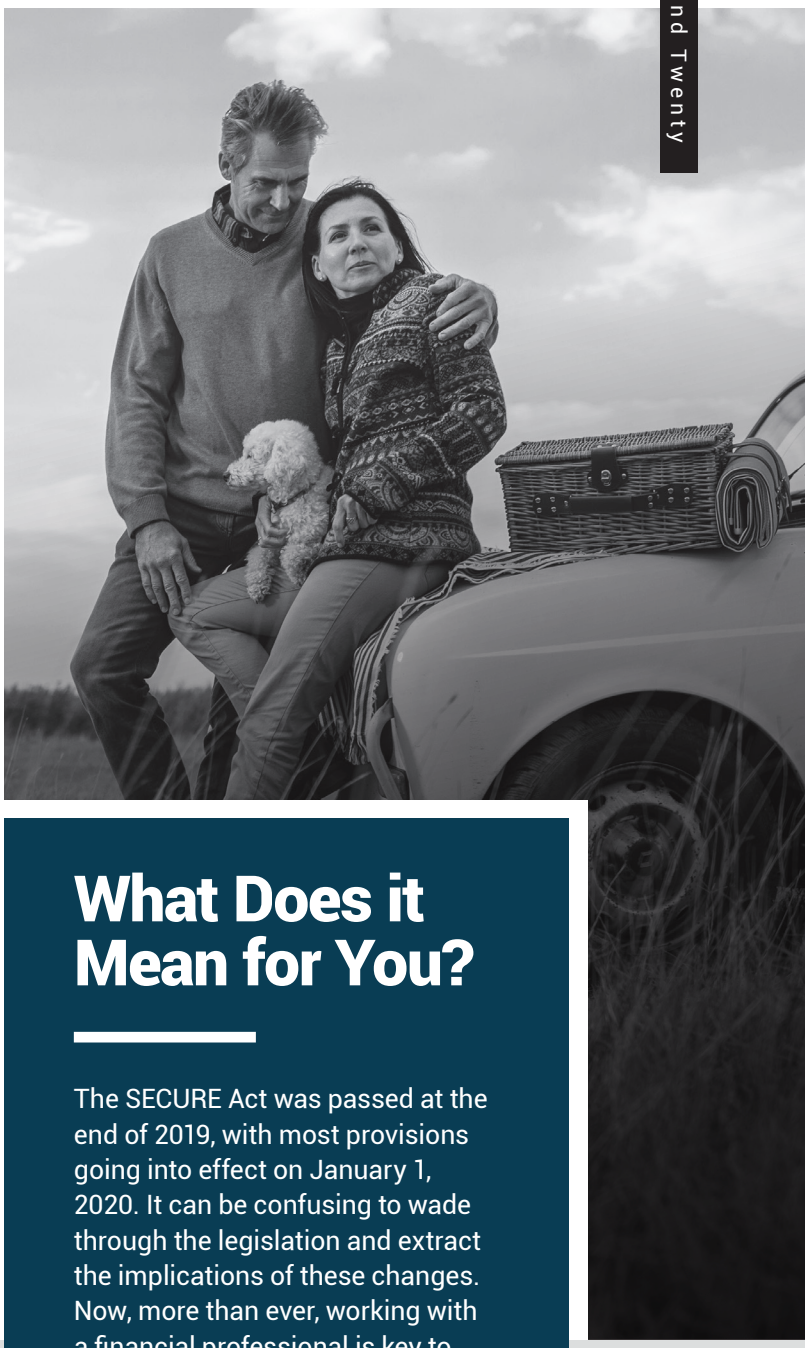
The

SECURE Act

Two Thousand and Twenty

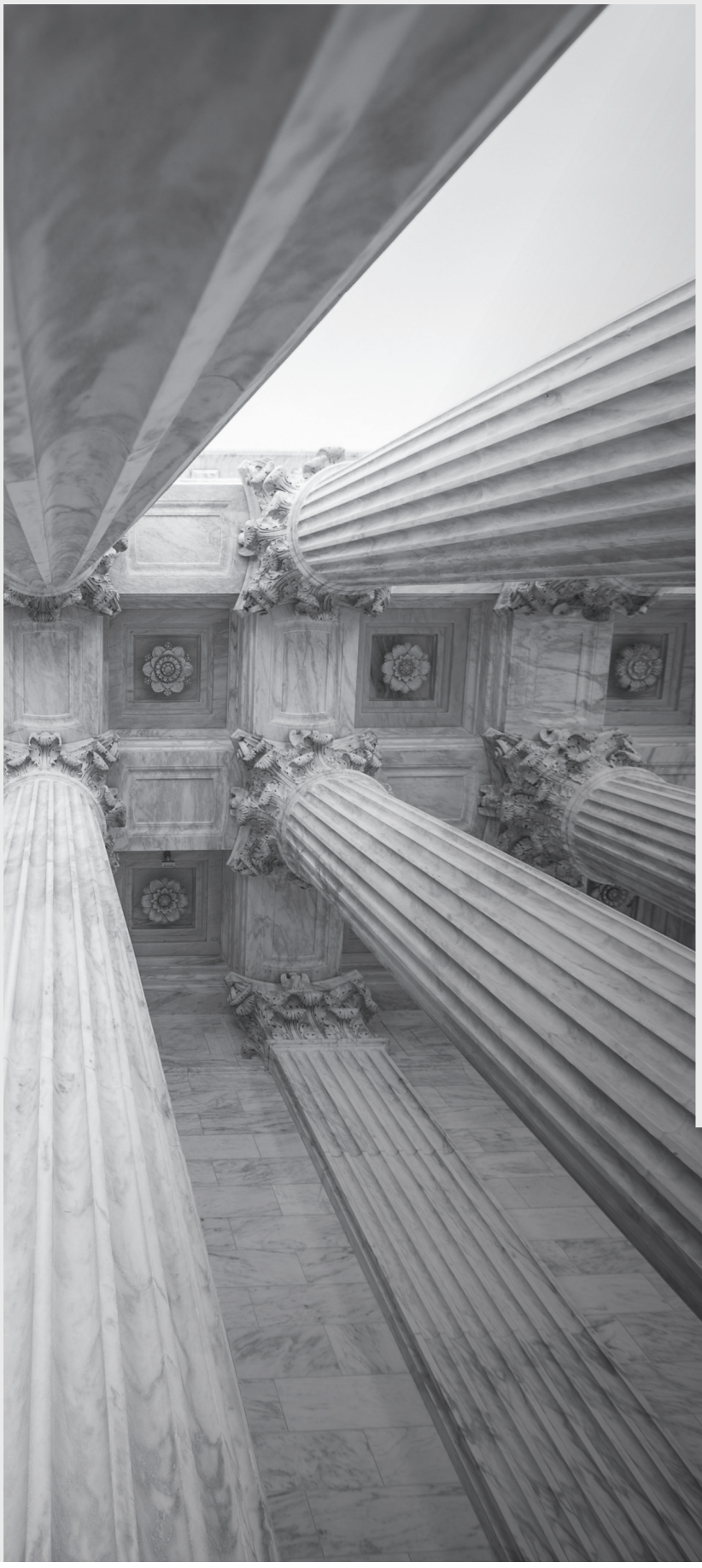


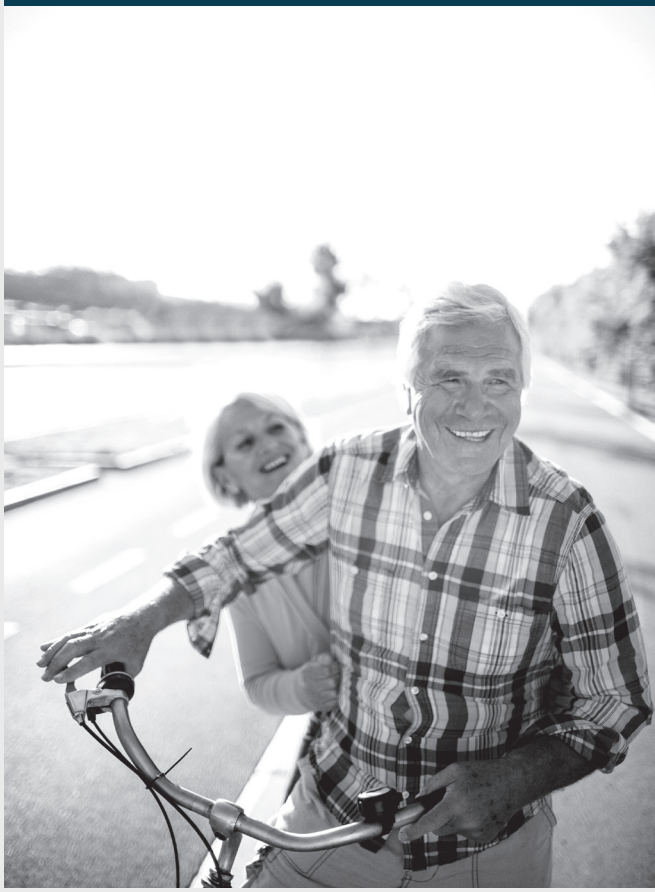
What Does it Mean for You?

The SECURE Act was passed at the end of 2019, with most provisions going into effect on January 1, 2020. It can be confusing to wade through the legislation and extract the implications of these changes. Now, more than ever, working with a financial professional is key to determining whether the SECURE Act could change your financial strategy going forward. Meanwhile, for an overview of what to expect from this new legislation, read on.

Davis Wealth Management, LLC

Plan, Protect and Preserve...Peace of Mind





Explaining the SECURE Act

"SECURE" stands for "Setting Every Community Up for Retirement."

The bill is intended to provide additional incentives to help people save more for retirement over a longer period of time, among other changes. The ideas behind the SECURE Act had been worked on for years before they were folded into a broader spending bill in late 2019. The bill passed on December 20, 2019, thirteen years after the Pension Protection Act of 2006, the last time such dynamic changes were made.[1]

Changes to Retirement Accounts

The most sweeping and widely discussed changes brought about by the SECURE Act were how retirement accounts were affected.

These changes included changing the age for taking Required Minimum Distributions (RMDs), which may allow for some individuals to continue saving for retirement over a longer period of time. However, financial strategies, like Stretch IRAs, were also affected. Let's explore these in more detail.[2]

Limits on Stretch IRAs

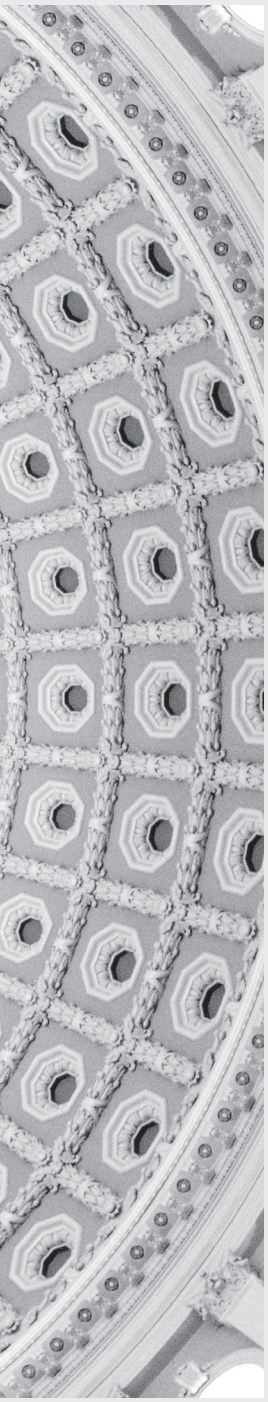
The legislation "modifies" the Required Minimum Distribution rules in regard to defined contribution plans and Individual Retirement Account (IRA) balances upon the death of the account owner.

Under the new rules, distributions to non-spouse beneficiaries are generally required to take place by the end of the 10th calendar year following the year of the account owner's death.[3]

It's important to highlight that the new rule does not require the non-spouse beneficiary to take withdrawals during the 10-year period. But all the money must be withdrawn by the end of the 10th calendar year following the inheritance.

A surviving spouse of the IRA owner, disabled or chronically ill individuals, individuals who are not more than 10 years younger than the IRA owner, and children of the IRA owner who have not reached the age of majority may have other minimum distribution requirements.

Let's say that a person has a hypothetical $1 million IRA. Under the new law, their non-spouse beneficiary may want to consider taking at least $100,000 a year for 10 years regardless of their age. For example, say you are leaving your IRA to a 50-year-old child. They must take all the money from the IRA by the time they reach age 61. Before the rule change, a 50-year-old child could "stretch" the money over their expected lifetime, or roughly, 30 more years.



IRA Contributions and Distributions

Another major change is the removal of the age limit for traditional IRA contributions.

Before the SECURE Act, you were required to stop making contributions at age 70½. Now, you can continue to make contributions as long as you meet the earned-income requirement.[4]

Also, as part of the act, you are mandated to begin taking required minimum distributions (RMDs) from a traditional IRA at age 72, an increase from the prior age of 70½. Allowing money to remain in a tax-deferred account for an additional 18 months (before needing to take an RMD) may alter some previous projections of your retirement income.[4]

The SECURE Act's rule change for RMDs only affects Americans turning 70½ in 2020 and beyond. For these taxpayers, RMDs will become mandatory at age 72. If you meet this criterion, your first RMD won't be necessary until April 1 after your 72nd birthday.[4]

Conduit Trusts

Before the SECURE Act, a Conduit Trust was an easier way to safeguard the life of an inherited IRA.

Instead of making an individual the beneficiary of the IRA, the trust would become the beneficiary. If you were concerned about how your heirs might spend their inheritance, putting your IRA into a conduit trust was one approach to help manage distributions.[5]

Under the SECURE Act, if the beneficiary of a conduit trust does not qualify as an eligible designated beneficiary (EDB), then the entire plan balance is required to be distributed by the 10th anniversary of the plan holder's death. The end result of this is that the previous benefits of the conduit trust might be limited to the new 10-year rule.[5]

Keep in mind, a trust involves a complex set of tax rules and regulations. Before moving forward with a conduit trust or any other trust, you'd be wise to work with a professional who is familiar with these rules and regulations.[6]

Annuities

This might be the most complicated part of the SECURE Act.

It's now easier for your employer-sponsored retirement plans to have annuities added to their investment portfolio. This was accomplished by reducing the fiduciary responsibilities that a company may incur in the event the annuity provider goes bankrupt. The benefit is that annuities may provide retirees with guaranteed lifetime income. The downside, however, is that annuities are often the incorrect vehicle for investors who are just starting out or far from retirement age.[7]

Businesses

In terms of wide-ranging potential, the SECURE Act may offer its biggest change in the realm of multi-employer retirement plans.

Previously, multiple employer plans were only open to employers within the same field or ones that shared some other "common characteristics." Now, small businesses have the opportunity to buy into larger plans alongside other small businesses, without the prior limitations. This opens small businesses to a much wider field of options.[8]

Another big change for small-business employer plans comes for part-time employees. Before the SECURE Act, these retirement plans were not offered to employees who worked fewer than 1,000 hours in a year. Now, the door is open for employees who have either worked 1,000 hours in the space of one full year or to those who have worked at least 500 hours per year for three consecutive years.[9]

College Students

For those who have graduate funding, the SECURE Act allows students to use a portion of their income to start investing in retirement savings.

The SECURE Act also contains a clause to include "aid in the pursuit of graduate or postdoctoral study." A grant or fellowship would be considered income that the student could invest into a retirement vehicle.[10]

One other provision of the SECURE Act: you can use your 529 Savings Plan to pay for up to $10,000 of student debt. Money in a 529 Plan can also be used to pay for costs associated with an apprenticeship.[11]

Changes for Families

Are you having a baby or adopting?

Under the SECURE Act, you can withdraw up to $5,000 per individual, tax free, from your IRA to help cover costs associated with a birth or adoption. However, there are stipulations. The money must be withdrawn within the irst year of this life change. Otherwise, you may be open to the tax penalty.[12]

Conclusions

The SECURE Act changed the landscape of retirement savings and may necessitate changes to your financial strategy. Let's work together to make sure that you are optimizing what's available and taking full advantage of the new rules. As always, you are welcome to reach out with any questions.

Footnotes, disclosures, and sources:

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Sources

1. Forbes, January 10, 2020.
2. WaysAndMeans.House.gov, April 2, 2019.
3. Forbes, December 29, 2019.
4. JD Supra, December 23, 2019.
5. WaysAndMeans.House.gov, 2019.
6. MarketWatch, January 9, 2020.
7. MarketWatch, January 16, 2020. The guarantees of an annuity contract depend on the issuing company's claims-paying ability. Annuities have contract limitations, fees, and charges, including account and administrative fees, underlying investment management fees, mortality and expense fees, and charges for optional benefits. Most annuities have surrender fees that are usually highest if you take out the money during the initial years of the annuity contact. Withdrawals and income payments are taxes as ordinary income. If a withdrawal is made prior to age 59½, a 10% federal income tax penalty may apply (unless an exception applies).
8. WaysAndMeans.House.gov, 2019.
9. MarketWatch, December 21, 2019.
10. Forbes.com, December 23, 2019. A 529 plan is a college savings plan that allows individuals to save for college on a tax-advantaged basis. State tax treatment of 529 plans is only one factor to consider prior to committing to a savings plan. Also, consider the fees and expenses associated with the particular plan. Whether a state tax deduction is available will depend on your state of residence. State tax laws and treatment may vary. State tax laws may be different than federal tax laws. Earnings on nonqualified distributions will be subject to income tax and a 10% federal tax penalty.
11. Forbes, December 23, 2019.
12. Congress.gov, May 23, 2019.

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