Bond INFORMATION MEMO

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The SECURE Act of 2019

On Thursday, December 19, 2019, the Senate voted in favor of an omnibus spending bill that includes some of the most significant retirement reform to take place in more than a decade. This reform comes in the form of the Setting Every Community Up for Retirement Enhancement Act, or the "SECURE Act" for short. The Act was signed into law by the President on Friday and will begin to impact many individuals' retirement and estate plans as early as January 1, 2020.

What is the SECURE Act?

In response to improving life expectancy and an increased number of individuals remaining in the workforce into their 70s, the SECURE Act makes several major changes to the way Americans will plan for retirement.

Among these changes, the Act eliminates the age cap prohibiting working individuals from contributing to traditional IRAs after the age of 70½ and increases the age that individuals are required to take minimum distributions (RMDs) from 70½ to 72 (allowing for an additional 1½ years of tax deferred saving).

The Act also includes wide-ranging provisions that: make 401(k) plans more accessible for small businesses; allow certain long-term part-time workers to participate in 401(k) plans; and allow penalty-free withdrawals for new parents, with certain restrictions.

The Cost? – Eliminating the "Stretch IRA"

One of the most significant changes made by the SECURE Act, is the elimination of the planning strategy known as the "Stretch IRA." This strategy permitted a non-spouse IRA (or Roth IRA) beneficiary to "stretch" the distribution of an inherited IRA over his or her fixed life expectancy. This was a powerful tax-deferral strategy for traditional IRAs as it permitted beneficiaries to minimize the amount of taxable income from taking distributions while remaining funds continued to compound tax deferred within the IRA.

The Act eliminates the Stretch IRA by requiring full-distribution of inherited IRAs (and Roth IRAs) by the end of the 10th year after the account owner's death. In addition to increasing tax exposure for distributions, it is also anticipated that the 10-year limit will push larger RMDs into the highest income years and thus, the highest tax years of a beneficiary's life.

Congress expects that the elimination of the Stretch IRA will raise nearly $16 Billion in tax revenue, and is expected to fund, in large part, the other changes made by the Act.

Who is Affected by the Elimination of the "Stretch IRA"?

With a few exceptions, the 10-year limitation will apply to IRA (and Roth IRA) beneficiaries where the account holder dies on or after January 1st, 2020. This includes individuals who are the beneficiaries of "see-through" or "conduit" trusts. Similar to the 10-year limitation applicable to an individual, if a "conduit" trust is named as beneficiary, a full payout of the account, and thus the distribution to the beneficiary, must occur within 10 years, as opposed to payments over the trust beneficiary's life expectancy. Therefore, a conduit trust will provide the beneficiary with access to the IRA funds much sooner than under prior law. If this is not acceptable, naming a "conduit" trust as beneficiary should be reconsidered.

Beneficiaries who were already taking advantage of the Stretch IRA because the account holder passed away in 2019 or earlier, are not subject to the 10-year limitation. However, if those beneficiaries die before the complete distribution of the account, the subsequent beneficiaries will be subject to the 10-year limitation.

Additionally, the 10-year limitation will not apply to a beneficiary who is a surviving spouse, minor child (but not a grandchild), disabled or chronically ill individual, or an individual who is no more than 10 years younger than the account holder. With the exception of minor children, these individuals will continue to be able to take distributions over their life expectancy. For minor children, the 10-year rule will apply, but only after the child reaches the age of majority.

Conclusion

In light of the SECURE Act and particularly its elimination of the Stretch IRA, this may be a good time to review your estate and retirement plans with your tax, financial and legal advisors. While there are alternatives to beneficiary designated traditional IRAs and Roth IRAs available, it is likely that mitigating the impact of the SECURE Act may require a combination of strategies.

If you have any questions about this new law, we encourage you to contact any of the attorneys in our Trusts and Estate Practice or the attorney in the Firm with whom you are regularly in contact.