SECURE Act Update

RMDs under the SECURE Act

The Setting Every Community Up for Retirement Enhancement Act of 2019 (SECURE Act) established a date dependent system for regulating required minimum distributions (RMDs).

- People who reached 70½ or inherited accounts for which the death occurred prior to 2020 are grandfathered under the old rules. The old rules are of little importance for test purposes.
- People who were not at least 70½ prior to 2020 are subject to the new rules. The new rules are of extreme importance for test purposes. Because there are still some questions that need to be resolved by the IRS about these rules, it is expected that questions under the SECURE Act will be more on the broad outlines than the detailed intricacies.

SECURE Act RMD Rules for the Owner of a Retirement Account or IRA

The SECURE Act changed the required beginning date (RBD) from 70½ to 72 for those who were not already 70½ by the end of 2019. The RBD for these people is now April 1 of the year following the year the person turned 72. The year a person reaches 72 is called the "trigger year." Under the old rules, some people were 70 in their trigger year and others were 71. Now everyone with a trigger year at age 72 uses the Table III (Uniform Table) life expectancy for age 72.

SECURE Act RMD Rules for Those Who Inherit a Retirement Account or IRA in 2020 and later

The rules for inherited retirement accounts and IRAs for deaths in 2020 and later were substantially modified; however, they maintain the general structure and thought processes of the old inherited RMD rules. The keys remain what type of person gets the retirement account and when the original owner died relative to his or her required beginning date (RBD). Some categories of beneficiaries may continue to stretch the inherited retirement money under the same rules as before. However, the SECURE Act was mostly designed to force money out of inherited retirement accounts (IRAs and employer defined contribution plans) by December 31st of the year containing the 10th anniversary of the deceased owner's death. Here is how to think about the new RMD rules for inherited IRAs and employer retirement accounts.

1. What category of person is inheriting the retirement account? Is the person or entity a "beneficiary," "designated beneficiary," or "eligible designated beneficiary"? These definitions are critical.
   a. ***Beneficiary.*** Being a beneficiary allows the person or entity to receive the retirement asset after the death. However, if a person or entity is only a beneficiary, then the RMD rules are the most severe. The rules for a situation without a designated beneficiary were not changed under the SECURE Act. Being a beneficiary (only) means the entity receiving the money does not have a life expectancy. The primary examples are estates and charities. Certain types of trusts are also in this category, but trust situations are not

expected to be testable for 2020. A major point is that an estate or charity is not a person with a measurable life. Thus, the old rules apply.

b. ***Designated beneficiary.*** A designated beneficiary is a person or "see through trust." These people have a life expectancy. Prior to the SECURE Act, a designated beneficiary was the person whose age went into the considerations for how long the retirement account could be stretched. For deaths in 2020 and later, the SECURE Act retained the term "designated beneficiary," but untethered it from using the life expectancy to determine the length of the stretch unless the beneficiary is an "eligible designated beneficiary" (defined below). Being a designated beneficiary (only) means the retirement account can only be stretched to December 31 of the year containing the 10th anniversary of the decedent owner's death. The identity of a designated beneficiary is still determined on September 30th of the year following the year of death. The RMD for a designated beneficiary is December 31 of the year with the tenth anniversary of the death.

c. ***Eligible designated beneficiary (EDB).*** For this very important category of beneficiaries, the EDB's age may play a part in determining the stretch. Also, only an EDB can stretch the retirement account longer than 10 years. There are two categories of EDB: surviving spouses and people who are not surviving spouses. Essentially, the SECURE Act did not change the rules for these people. Also, the eligibility for an EDB is established on the decedent's date of death even though the designated beneficiary portion is still determined on September 30th of the year following the year of death.

   i. A surviving spouse EDB: Only the surviving spouse has the option to move the decedent's retirement account into a retirement account owned by the surviving spouse and thus treated as if the person was the original owner of the money. The surviving spouse EDB also has the same other options as other EDBs.

   ii. Nonsurviving spouse EDBs include a beneficiary who is not more than 10 years younger than the decedent owner (for example, a sister who is two years older or a friend who is eight years younger); a long-term disabled person; a chronically ill person; or the decedent's minor child (until the child reaches the state-set age of majority, at which time the 10-year rule kicks in).

Table 1: RMDs at a Glance (for the original owner in 2020 and later)

Plan Type	RMD Factor	RMD Start Date	Aggregation Allowed
IRA	Uniform Lifetime or Joint Life and Last Survivor Expectancy table	Age 72	Yes—with other IRAs only
Roth IRA	No RMD required	None	N/A
403(b)	Uniform Lifetime or Joint Life and Last Survivor Expectancy table	Age 72 or year of retirement, if later (5% or more owner must start at 72)†	Yes—with other 403(b) accounts
401(k) or other qualified plans	Uniform Lifetime or Joint Life and Last Survivor Expectancy table	Age 72 or year of retirement, if later (5% or more owner must start at age 72)	No

Plan Type	RMD Factor	RMD Start Date	Aggregation Allowed
Roth 401(k)	Uniform Lifetime or Joint Life and Last Survivor Expectancy table	Age 72 or year of retirement, if later	No

*If you inherit a retirement account from your spouse, you may elect to treat the account as your own. If you make that election, that account would no longer be treated as an inherited account. Special rules apply if a trust, estate, or other nonhuman entity inherits a retirement account. Please consult a tax adviser.

† Special rules apply to amounts accrued in a 403(b) plan prior to 1987.

Table 2: Required Minimum Distributions for IRA Beneficiaries

	Spouse Only	Nonspouse Eligible Designated Beneficiary†	No Designated Beneficiary (including an estate, charity, or some trusts)
IRA owner dies on or after Required Beginning Date	Spouse may treat as their own, Or Distribute over spouse's life using Table I* ▪ Use spouse's current age each year Or Distribute based on owner's age using Table I ▪ Use owner's age as of birthday in year of death ▪ Reduce beginning life expectancy by 1 for each subsequent year ▪ Can take owner's RMD for year of death	Distribute using Table I ▪ Use younger of 1) beneficiary's age or 2) owner's age at birthday in year of death ▪ Determine beneficiary's age at year-end following year of owner's death ▪ Reduce beginning life expectancy by 1 for each subsequent year ▪ Can take owner's RMD for year of death	Table I ▪ Use owner's age as of birthday in year of death ▪ Reduce beginning life expectancy by 1 for each subsequent year ▪ Can take owner's RMD for year of death
IRA owner dies before Required Beginning Date	Spouse may treat as their own Or Take entire balance by end of 5th year following year of death Or Distribute based on Table I ▪ Use spouse's current age each year ▪ Distributions do not have to begin until owner would have turned 72	Take entire balance by end of 5th year following year of death Or Distribute based on Table I ▪ Use beneficiary's age at year-end following year of death ▪ Reduce beginning life expectancy by 1 for each susbsequent year	Take entire balance by end of 5th year following year of death

* Table I – Single Life Expectancy, Publication 590

† Those who are only a designated beneficiary are under the 10-year rule regardless of when the decedent passed away.

Additional notes on Table 2: Early in 2020, there are some elements of this table that will require further guidance from the IRS.

1. For designated beneficiaries only (not EDBs), for deaths on or after the required beginning date there is some uncertainty if there is an option to continue RMDs using the deceased's life expectancy.
2. How the state sets the age of majority for EDBs who were minor children is unknown. Is it the voting age? Is it the UTMA age? Further guidance is needed from the IRS.

SECURE Act and Lifetime Income Benefits

The SECURE Act tries to advance lifetime income options for retirees as an alternative/”look-alike” to defined benefit plans. The Act provides for portability of lifetime income options for defined contribution plans, 403(b) plans, and governmental 457 plans (457(b) plans). There are also safe harbor rules for plan fiduciaries selecting lifetime income providers as long as the fiduciary engaged in an objective, thorough, and analytical approach involving the financial capacity of the insurer to satisfy the guaranteed income contracts and considers the costs and benefits of the insurance company offerings. If the fiduciary concludes that the insurance company at the time of selection is financially capable of meeting its obligations and the relative cost and benefits of the guaranteed retirement income contracts are reasonable, then the fiduciary safe harbor is met and the fiduciary is not liable for the initial selection of the retirement income provider. On the other hand, fiduciaries certainly need to monitor the financial state of the lifetime income providers. Thus, the SECURE Act really only offers fiduciary liability relief for the initial selection. In truth, even this liability protection is only as good as the thoroughness of the search and the documentation thereof because the lawsuit will allege that the fiduciary was not thorough enough. Still, at least the bar has been set.

One thing the lifetime income rules have in common is that they allow workers to have a better feel for how much income their current situation would provide in retirement. For example, most people would not know how much monthly income could reasonably be expected from a retirement account worth $100,000 at retirement. For most Americans this sounds like a lot of money. However, the lifetime monthly benefit should be somewhere between $300–$600/month, depending on whether or not it is annuitized. Also, if this $100,000 is 20-30 years in the future, then the purchasing power of the amount is roughly cut in half. A lifetime income option would be somewhere near this range and hopefully the worker will be motivated to increase contributions. The DOL has until December 2020 to come up with model lifetime income disclosure language.

Other SECURE Act Issues

- Traditional IRA contributions can now be made at any age as long as there is earned income. This starts for the tax year 2020. It is not available for the tax year 2019, not even for contributions made in 2020 that are coded as 2019 contributions. In other words, someone older than 72 in 2020 cannot make a 2019 contribution in 2020.
- Retirement loans cannot offer credit cards or similar arrangements for retirement plan loans.
- Penalty-free withdrawals from employer retirement plans and IRAs up to $5,000 per parent per event for the birth or adoption of a child. Also these withdrawals can be repaid to the IRA or employer retirement plan later. Income on the distribution is still taxed. The details on how repayments will be handled have not been announced. Parents have one year after the exact date of the birth or adoption to take the distribution. If they take the distribution any time before the birth or adoption, these rules don’t apply and the distribution will be subject to the 10% early withdrawal penalty system.
- Up to $100,000 per disaster can be distributed from retirement accounts for “qualified disaster distributions.” These distributions are exempt from the 10% early withdrawal penalty.
- 7.5% of AGI replaces 10% of AGI for 2020 as an exception to the 10% early withdrawal penalty.

- The SECURE Act extended the deadline for adopting a new retirement plan to the due date for filing that year's tax return, plus extensions. Now all plans are like SEPs.
- Defined benefit and 457(b) (governmental 457 plans) may allow in-service distributions starting at 59½.
- Automatic enrollment plans are now capped out at 15% instead of 10% for years after the first year.

Income Tax Issues

- The kiddie tax rules return to the parents' marginal tax rate instead of the trust and estate tax rates.
- Up to $10,000 of 529 plan withdrawals can be used to pay the student debt of the 529 beneficiary or a sibling (brother, sister, stepbrother, stepsister). This is a cumulative lifetime limit on the 529 account for each person. For example, an individual can withdraw $10,000 from the 529 they are a beneficiary of to pay off their own student debt in 2020. The individual cannot take any more for the rest of their life as a qualified distribution to pay their student debt, but they can take up to $10,000 each for all their other siblings (assuming their siblings have not taken any 529 distributions to pay their qualified student debt).
- Qualified 529 distributions can be made for fees, books, supplies, and equipment for apprenticeship programs.
- The discharge of qualified principal residence debt remains excluded from gross income in 2020.
- The energy-efficient homes credit is extended through 2020.
- Credits for health insurance costs for eligible individuals is extended through 2020.
- Two taxes from the Affordable Care Act were permanently repealed: the medical devices tax and the "Cadillac tax" on certain high cost employer-sponsored health insurance coverage.
- Qualified mortgage insurance premiums may be deducted as if they are mortgage interest for 2018–2020.
- Qualified tuition payments may be deducted for 2018–2020.
- The credit for certain small employers starting an employer retirement account has been increased. The old credit was $500/year for three years for eligible employers with no more than 100 employees making $5,000/year or more. The new credit is the lesser of 50% of the qualified plan start-up costs or the greater of $500 or $250 times the number of nonhighly compensated employees eligible to participate in the plan.
- The SECURE Act extended the deadline for adopting a new retirement plan to the due date for filing that year's tax return including extensions. Now all retirement plans are like SEPs in that they can be established after the year has ended. Of course, this limits the effectiveness for the first year if the employees are expected to be contributing, such as with a 401(k), but it helps the employer contribution plans.
- Starting in 2021, multiple employers can join together under one plan document even if they are completely unrelated. Congress hopes this will encourage more employers to offer retirement plans to their workers. Multiemployer plans have been available for a long time; however, there had to be a "nexus" between the employers (meaning the employers were related in some manner, such as

being in the same industry), and if one employer failed the plan requirements then all employers in the plan also failed. Starting in 2021, the need for a nexus is eliminated, and if one of the employers fails the plan requirements, then the other employers are safe as long as they actually meet the plan requirements. The hope is that multi-employer plans will lower administrative costs for the various employers. This could be especially true with the use of the Internet. It is possible to accommodate many plan participants with a broader use of the Internet for things like enrollment and contribution changes, etc.

- The SECURE Act started the process to allow long-term part-time workers to be part of cash or deferred arrangements ("CODAs," like 401(k) plans). Starting in 2023, employees who are at least 21 and have three consecutive years of service with more than 500 hours but less than 1,000 hours per year will be eligible for the retirement plan; however, they can be denied matching funds and nonelective employer contributions. Also, they will not count for nondiscrimination testing or top-heavy testing. In other words, they will be allowed to save using the employer plan, but the employer is not really required to count them for most tests. Also, these employees get a year of vesting for every 1,000 hours of work. If they work 1,000 hours in a year, they are no longer in this category. Finally, the first year that will count toward the three-year rule is 2021. Thus, no one will be helped by this law until 2024.