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Washington's SECURE Tax Act

Somebody Was Working Over the Holidays

While we all enjoyed the time over the holidays with friends and family, Congress quietly passed a major retirement bill that may affect you, your financial planning, and the retirement planning landscape.

The bill was introduced to the House back in May of 2019 and passed with overwhelming support, 417 – 3 and yet was not widely discussed within the planning community. The bill faced some opposition in the Senate and underwent several additions, retractions, and addendums before finally passing on December 19th as part of a fiscal appropriations bill for 2020.

The cleverly named SECURE, or the Setting Every Community Up for Retirement Enhancement Act, is the second largest tax package passed by the Trump administration behind the Tax Cuts and Jobs Act, which was passed at the end of 2017. The SECURE Act introduces a host of changes for IRAs and retirement plans providing some important planning opportunities. We discuss a few of the new provisions below. We've elaborated on two topic areas that may mean changes are necessary to your current financial plans (or to the plans of your parents or others you know). Rest assured, your advisor team is up to speed on the various nuances of the new law and we look forward to discussing them with you at our next meeting.

Some IRAs Can Now Wait To Age 72

Here is the great news: It just got a lot easier to figure out when you need to take your IRA's first required minimum distribution (RMD).

For those of you age 70 ½ and older, or if you are the beneficiary of an inherited IRA, you're likely aware that Vista makes sure your RMDs are made timely. For those of you who aren't familiar with RMDs, traditional and Rollover IRAs are required to eventually make distributions based on formulas set by Congress. The idea being that taxes on the accounts' growth can't be deferred forever.

The SECURE Act sets the RMD age at 72 instead of 70 ½ (the first RMD must be taken by April 1st of the year following your 72nd birthday). If you are currently 70 or 71 years old and have already begun your RMDs, you will continue to take distributions each year. You are not allowed to stop your minimum distribution for the year and begin again at age 72.

Planning Points:

- **Roth Conversions.** Consider Roth conversions in years post-retirement but prior to Social Security and RMD age, when income is low. Note also that delaying IRA distributions in early retirement may provide you an additional opportunity to complete Roth conversions in low tax years.

- **IRA Contributions.** Under the old law taxpayers could not contribute to IRAs after age 70 1/2. Under the new SECURE Act, you may contribute to IRAs regardless of your age as long as you have earned income.

IRAs Can't Stretch Like They Used To

If you inherited an IRA or qualified retirement account and you were not the decedent's spouse, you were required to take distributions each year.

However, by designing the account as a “Stretch” IRA under previous law, you could take distributions based on your life expectancy, stretching distributions out perhaps 30 to 50 years. Distributions each year would have been minimal, and the account would have been able to grow, largely keeping its tax-deferred status.

The SECURE Act eliminates Stretch IRAs from being set up and will require many, but not all beneficiaries, to withdraw the balance of future inherited IRAs within ten years. Note that withdrawals over the new 10-year period don't have to be ratable, so there is a tax planning opportunity here. Most beneficiaries, including spouses and disabled individuals, may still stretch an inherited IRA over their expected life under the SECURE Act. Existing stretch IRAs that have been making their RMDs are not affected by the Act.

Stretch IRAs were a great estate planning tool because they could pass to heirs with minimal tax and continue to grow tax-deferred while making small distributions. The SECURE Act requires us to think about inherited IRAs much differently. Consider this example: Adult children who are in their prime earning years who inherit IRA assets from a deceased parent. The children's high wages, coupled with a large IRA distribution in a single year, will result in a higher tax bill. However, multipleyear tax planning may help to minimize taxes paid over the 10-year period.

Planning Points:

- **Check your beneficiaries.** Who is going to inherit your IRA assets? If your child/children are the primary or contingent beneficiaries of IRA assets, you may want to make sure they are aware of the rules and have a plan in place.
- **Cash Flow and Tax Planning**. If you are the beneficiary of a recent decedent's IRA, we should develop a plan to optimize the timing of your distributions. For beneficiaries approaching retirement, it may be beneficial to take a lump sum in a low income year.
- **Review Trust Provisions.** IRA assets typically pass to beneficiaries directly instead of through your trust. If you name a trust as a beneficiary of an IRA, the funds will pass according to the instructions in that trust. If that is the case, your trust should be reviewed to avoid having the full RMD taken in year ten or to avoid having distributions subject to trust tax rates (which climb to a federal rate of 37% on income over $12,750).
- **Consider Roth Conversions.** Roth IRAs do not have RMD requirements. As the account owner of an IRA, you can convert your IRA assets to Roth, pay the tax now, and save your beneficiaries from a potentially large tax bill in the future.
- **Donate your IRA to Charity using a Charitable Remainder Trust (CRT)**. Create a CRT and name the charitable trust as the beneficiary of your IRA. You can name your child or other individuals as the **income** beneficiary of the CRT, spreading the distributions over the income beneficiary's life. When the income beneficiary dies, any remaining account balance in the CRT would then pass to a charity.
- **Purchase a life insurance policy.** If you donate your IRA directly to a charity (rather than using a CRT) but want to ensure your heirs are adequately made whole, consider purchasing a life insurance policy

that would pay out (potentially tax free) to your beneficiaries at your death.

Feeling SECURE Yet? Other Provisions...

Delaying RMDs and the elimination of the Stretch IRA are just some of the changes in the SECURE Act. Some of the other changes are included below.

401(k) Participation for Part-time Employees

The new rules make it easier for part-time employees to contribute to a company 401(k). Under the new law, taxpayers who work at least 500 hours with a company for three consecutive years, or 1000 hours in one plan year (the old rule), are eligible to contribute to a 401(k).

Annuities in Your 401(k)

Currently annuity options are only offered in 10% of all employer sponsored plans. The SECURE Act eliminates some negative provisions for employers who included annuities in their retirement plans. As a result, we may start to see more annuity options available. As with all aspects of retirement planning, we will be happy to advise you on any options in your retirement plans.

Qualified Birth or Adoption Distributions from IRA

Barring a list of exceptions that include hardship and separation from service, making withdrawals from an IRA prior to 59 ½ comes with a 10% early distribution penalty. The SECURE Act extends the 10% penalty exception to new parents, who can distribute $5,000 from each of their IRAs in the year of birth or adoption.

Use 529 Plan Assets to Pay Down Student Loans

The Tax Cuts and Jobs Act expanded the usage of 529 plan assets in 2017. Under that law, you could distribute up to $10,000 per year from a 529 for K-12 expenses (California did not conform and such distributions are subject to a penalty for California tax purposes). The SECURE Act allows a $10,000 lifetime distribution limit to pay down student loans.

Thanks

We hope this finds your 2020 off to a prosperous start and that you find the information in this letter useful. Of course, please be sure to always discuss any planning ideas with us and your other advisors before implementing them. As always, please contact us at your convenience with any comments or questions.

Thank you for the trust you've placed in Vista.

Your Vista Wealth Management Team

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