<u>The SECURE Act: What It Does and What It Can Mean For Your Estate Plan</u>

Near the end of 2019, the Senate passed a budget reconciliation bill that included the Setting Every Community Up for Retirement (SECURE) Act. Effective as of January 1, 2020, this bill substantially changes existing law regarding retirement plans, such as 401(k)s, IRAs, and Roth IRAs. The SECURE Act made several changes to existing law with respect to retirement accounts, but one change has generated a great deal of attention and concern among estate planners with respect to clients' retirement accounts – the substantial shrinking of the period over which many beneficiaries may withdraw assets from an inherited retirement account.

Under previous law, "designated beneficiaries" (individuals or certain trusts) were permitted to withdraw funds from the account over the beneficiary's remaining life expectancy. If the retirement plan beneficiaries included anyone who was not a designated beneficiary, the entire account balance had to be withdrawn at a time of the beneficiary's choosing, but not later than 5 years after the original account owner's death. A designated beneficiary was required to withdraw the RMD each year, using IRS tables to determine the percentage to be applied. This allowed a beneficiary to spread out the income tax hit (in the case of pre-tax plans, such as a traditional IRA) or maximize the beneficiary's ability to enjoy tax-free growth for the assets held in the account.

Effective for retirement accounts inherited from an employee who died January 1, 2020 or later, the SECURE Act changed this by eliminating the ability of various beneficiaries to use life expectancies in determining the RMDs. A select number of designated beneficiaries, now referred to as "eligible designated beneficiaries," can continue to use their life expectancies for RMD purposes. These eligible designated beneficiaries are the account owner's spouse, the account owner's minor child, a disabled individual, a chronically ill individual, or anyone not more than 10 years younger than the account owner. However, minor children will be required to withdraw RMDs calculated over their life expectancies only until reaching age 18, at which point the RMDs will cease and the child will be required to withdraw the remaining balance of the retirement account within 10 years of becoming an adult. All other designated beneficiaries are required to withdraw the entire balance of the retirement plan account within 10 years of the original account owner's death (like the 5-year withdrawal requirement for non-designated beneficiaries under the previous law). The rules governing distributions to non-designated beneficiaries (the 5-year requirement) remain unchanged. In addition, as under the prior law, if an account owner names his or her spouse as the beneficiary of an IRA, the spouse can "roll over" the IRA to the spouse's own IRA and use the spouse's life expectancy in calculating RMDs.

The change in the determination of RMDs for many beneficiaries of an inherited retirement account may require advisors and their clients to rethink how retirement accounts should be handled in each particular estate plan. For example, if an IRA account owner previously named a trust for a grandchild as a beneficiary of a portion of the IRA, with RMDs required to be distributed from the trust to the grandchild each year for the grandchild's life expectancy (as was frequently the case under pre-SECURE Act law when leaving a retirement plan account in a trust), the fact that the IRA is now required to be distributed within 10 years to the grandchild may not be what the account owner wants.

On the other hand, making IRA distributions from the trust to a beneficiary discretionary, rather than mandatory, may have negative federal income tax consequences, possibly further affecting the account owner's intentions. Trusts reach the highest income tax bracket much earlier than individuals do (a trust will reach the highest tax bracket after earning $12,950 of income in 2020). A handful of proposals to reduce the tax burden have been suggested by advisors, but each will require tradeoffs when compared to the treatment of inherited retirement plans under prior law. In light of the potentially considerable effects of the SECURE Act on estate plans, it is a good idea for each client with a substantial retirement plan to speak with an advisor about the ramifications for the client's current estate plan, explore the various options that exist, post-SECURE Act, and find a solution to accomplish the client's objectives in light of this new law.

If you have any further questions about the impact that the SECURE Act will have on your estate plan, or if you wish to discuss options to accomplish your estate planning goals, please contact us at (239) 436-1500 to set up an appointment.

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