The SECURE Act: What Plan Participants and Beneficiaries Must Know

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The following article was featured in the January 2020 edition of *Legacy*, the Vorys newsletter focused on wealth planning.

In late December, 2019, the "Setting Every Community Up for Retirement Enhancement Act," or the "SECURE Act," was enacted. The SECURE Act makes dramatic changes to the law relating to defined contribution plans (such as 401(k) plans), defined benefit pension plans, and individual retirement accounts (IRAs). These changes impact financial planning and estate planning for retirement benefits. Some of the changes are taxpayer friendly, but there are also changes that accelerate income tax liabilities for beneficiaries. Below are some of the highlights.

THE GOOD NEWS:

Age 72 is the new age 70½

Under prior law, plan participants and IRA owners who had reached age 70½ were required to begin taking required minimum distributions (RMDs) from their retirement plans and IRA accounts. The SECURE Act increases the age for RMDs from age 70½ to age 72.

This age increase is effective for individuals who reached age 70½ *after* December 31, 2019. Individuals who reached age 70½ before December 31, 2019 are required to take RMDs in 2020 and beyond.

IRA contributions at any age

Under prior law, individuals 70½ and older were prohibited from contributing to a traditional IRA. The SECURE Act repeals this limit. Thus, beginning January 1, 2020, an individual may contribute to a traditional IRA at any age, as long as the individual has earned income for the year. Limitations apply as to the annual amount that can be contributed and to whether such amount is deductible.

THE BAD NEWS:

Partial Elimination of "Stretch-Out" Treatment

Under prior law, the RMDs that must be taken after the death of a retirement plan participant or IRA owner could, in many cases, be "stretched-out," or taken over the life expectancy of the designated beneficiary. Stretch-out treatment for such accounts was very tax-favorable, since the funds remaining in the retirement plan or IRA were able to continue to grow tax-deferred over the course of the beneficiary's life expectancy. The SECURE Act generally eliminates stretch-out treatment for designated beneficiaries (other than certain eligible designated beneficiaries) and implements a 10-year rule. The 10-year rule requires that the entire balance of the retirement plan or IRA be distributed within a 10-year period, ending on December 31st of the year that contains the 10th anniversary of the death of the plan participant or IRA owner.

Stretch-out treatment remains available if the designated beneficiary qualifies as an "eligible designated beneficiary," defined as:

- A surviving spouse;
- A minor child of the plan participant or IRA owner (but only until such minor reaches the age of majority);
- An individual who is disabled or chronically ill; or
- Any other individual who is not more than 10 years younger than the plan participant or IRA owner.

The changes under the SECURE Act apply to plan participants and IRA owners dying ***after*** December 31, 2019. *Thus, existing stretch IRAs may continue to be administered over the lifetime of the existing beneficiary. Upon the death of every existing beneficiary, however, the SECURE Act 10-year rule will become applicable.*

ACTION REQUIRED:

If you are a retirement plan participant or an IRA owner, you need to review your beneficiary designations and estate plan. Although each person's situation is different and must be analyzed separately, there are some general key takeaways:

1. If you designated only individuals as the primary and contingent beneficiaries of your retirement plan or IRA, then it is likely that no changes are needed to your estate plan to address the SECURE Act. A spouse may still elect a rollover or elect to take RMDs over his or her life expectancy. However, a non-spouse beneficiary, other than an eligible designated beneficiary, can no longer elect to stretch RMDs over his or her life expectancy, and the entire amount in the plan or IRA must be distributed to the beneficiary within the 10-year period.
2. If you designated your trust as a primary *or* contingent beneficiary of your retirement plan or IRA, then your trust must be reviewed to determine whether any changes need to be made to ensure your trust aligns with your intended goals.

a. If your trust contains a "conduit" feature, your trust will likely need to be changed. The conduit feature generally provides that all distributions from a retirement plan or IRA (including RMDs) received by the trust must immediately be distributed to the trust beneficiary. Prior to the SECURE Act, the conduit

feature: (1) minimized the income tax impact of RMDs by allowing a trust beneficiary to stretch-out RMDs over his or her life expectancy; and (2) allowed the trustee to control distributions from the plan or IRA.

After the enactment of the SECURE Act, the conduit feature likely has the opposite effect. If a conduit trust is named as beneficiary, the entire amount in the plan or IRA must be distributed to the beneficiary within the 10-year period (or potentially a 5-year period), unless the beneficiary is an eligible designated beneficiary. Thus, conduit trusts may no longer facilitate controlled payments of retirement plan or IRA balances over the designated beneficiary's life expectancy, making conduit trusts much less attractive going forward.

b. If your trust does not contain a conduit feature, it is considered an "accumulation trust," because distributions from a retirement plan or IRA (including RMDs) received by the trust are not required to be distributed to the beneficiary, but instead accumulate in the trust. If your trust is an accumulation trust, it may need to be changed to ensure that it is not subject to a special rule that would require the distribution of the entire balance of the retirement plan or IRA over a short 5-year period.

Please contact your Vorys attorney to learn more about how the SECURE Act directly affects you and your family, and whether your beneficiary designations and estate plan should be updated to account for the changes in the law.