Retirement Bombshell: The SECURE Act

Shortly before year end 2019 Congress passed some new legislation that will dramatically impact your retirement and ability to transfer retirement assets to your family. Included as an attachment to a year end spending bill, the Senate passed the 'Setting Every Community Up for Retirement' (or SECURE) Act. This legislation contains some significant changes that may change your planning for retirement.

The SECURE Act became effective on January 1, 2020, with various changes for the good and bad of those saving for retirement and the most effective way to pass wealth on to future generations. Here is a summary of the Act that might impact you:

Elimination of the "Stretch IRA

The Stretch IRA is a strategy to maximize the value of an IRA when it is left to non-spouse beneficiaries. When someone other than your spouse inherits an IRA they can transfer the IRA into an inherited IRA account to continue the tax deferral of the funds in the IRA. Starting in the year after the original IRA owner's death, the recipient of the inherited IRA is only obliged to receive a required minimum distribution each year based on their age. This allows them to stretch the inherited IRA over decades and possibly their lifetime. This strategy spreads out the payment of income tax on the IRA over an extended period of time which could have an amazing impact on someone who inherits an IRA by allowing the IRA to grow tax-deferred over their lifetime.

The SECURE Act has effectively eliminated the stretch IRA strategy by creating a new regulation in the tax code that requires all non-spouse beneficiaries to withdraw all of the funds from an inherited IRA within 10 years of receiving the IRA funds. The SECURE Act does include some exceptions to this rule. Surviving spouses, minor children, those chronically ill or disabled, and beneficiaries who are not more than 10 years younger than the deceased IRA owner may continue to stretch an inherited IRA.

Age Limit Eliminated for Traditional IRA Contributions

Prior to the SECURE Act passing, individuals were not eligible to make tax-deductible contributions to their IRA after reaching the age of 70½. The SECURE Act removed this age limit. Starting in 2020, any individual with earned income after the age of 70½ can continue to save for retirement by making contributions to their IRA.

Age Raised for RMDs

The income tax code requires all individuals with an IRA or employer retirement account to start taking a required minimum distribution (RMD) at a certain age. This requirement allows the federal government to start receiving income taxes on at least a portion of your tax deferred retirement savings. The SECURE Act raises the age for RMDs from 70½ to 72. This will allow individuals that do not need funds from their retirement accounts to stay invested longer and defer the payment of income taxes on their retirement savings.

For example, if your birthdate is December 15, 1949, you did not turn 70½ until March 15, 2020. Under the SECURE Act you will be able to defer your first RMD until you turn 72. Just like the previous rule, your required beginning date for your first RMD will be April 1 of the year following the year you turn 72. If you chose to wait to take the first RMD before April 1 in the calendar year following the year you turn 72 you will also need to take a distribution for being 73 in that same year. After the first year you are required to take a distribution each year within that calendar year. In this example you would need to take your first RMD by April 1, 2022. Please note this change does NOT apply to individuals who turned 70½ before December 31, 2019 (anyone born before June 30, 1949). These individuals will continue to take RMDs under the old rules.

The changes to the RMD age did not change the calculation method used for RMDs. At this point taxpayers will use the same IRS life expectancy factors table to calculate their RMD amount. The factors do not get pushed back. Instead, retirement account holders will not need to use the factors for ages 70 and 71. They will begin with the factor beginning at age 72. It is expected that the IRS will be updating the life expectancy factor table sometime soon, but there is no estimated date at this time.

IRA Charitable Rollovers Still Available at Age 70½

Despite the change of the age used to determine the year for your first RMD, the SECURE Act did not change the rules related to Qualified Charitable Distributions (QCDs). So even though IRA owners will not have to start taking RMDs from their IRA until they reach age 72, they are still able to make QCDs from an IRA once they reach the actual age of 70½.

An IRA owner can make a QCD of up to $100,000 per year directly from their IRA to a charity without any tax consequences. The amount distributed to a 501(c)3 charity is not deductible, but it also not reported as income. This strategy is very effective by using before tax dollars to make charitable donations and it can reduce your federal and state income taxes. Please note: a QCD can only be made from an IRA. It is not available from an employer retirement account, such as a 401(k), 403(b), or 457 plan.

Please call (800) 416-1655 if you want information, have questions, or would like to discuss using this strategy.