Stage Is Set for Significant Retirement Bill to Pass by Year End (SECURE Act)

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For several months, attorneys and tax practitioners have been following the so-called "SECURE" Act, which will greatly impact qualified retirement plans and individual retirement accounts (IRAs). While the Act passed the House of Representatives by a margin of 417 to 3 in May of this year, similar legislation stalled in the Senate. On Monday, in what can only be described as a last minute Hail Mary pass to get legislation in place by the end of the calendar year, the provisions of the SECURE Act were attached to a government appropriations bill. The bill introduced on December 16, 2019, must be taken up by Congress by this Friday, in order to avert the latest threatened government shutdown.

While there any many law changes impacting retirement plan sponsors contained in the Act, the most significant provisions of the legislation impacting individuals relate to the rules governing withdrawals from tax-deferred retirement accounts, including IRAs. The timing of such withdrawals is important, as amounts distributed from tax-deferred retirement accounts and non-Roth IRAs are subject to income tax when received by the account holder or designated beneficiary.

Two key provisions surrounding withdrawals that would change under the SECURE Act provisions are:

1. **Change in Beginning Date for Required Minimum Distributions.**

Under current law, most individuals are required to begin taking required minimum distributions from their own retirement plans or IRAs upon reaching age 70½. The proposed legislation will change the initial year of required distribution to age 72. Since few individuals have celebrated their "half birthdays" since their elementary school years, this is a modest step towards easing the understanding of the rules applicable to plan withdrawals. It also provides additional brief deferral of withdrawals for account holders who do not need the funds contained in their accounts for retirement living expenses.

1. **Elimination of Stretch Withdrawals from Inherited Retirement Accounts and IRAs.**

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While individuals may defer distributions from their own retirement accounts and IRAs to age 70½ under current law, the persons inheriting those accounts as designated beneficiaries may not defer distributions to that age unless they are a surviving spouse. Instead, non-spousal designated beneficiaries must commence receiving required minimum distributions no later than December 31st of the year following the original account holder's death, regardless of their age. While distributions must commence soon after the account holder's death, current law does permit such beneficiaries to stretch withdrawals from inherited accounts over their life expectancy. This has the effect of allowing the underlying account to continue to grow on a tax-deferred basis and also defers the ultimate payment of income tax on account withdrawals.

Under the SECURE Act, the distribution of funds from such inherited accounts would be limited to a ten-year period following the original account owner's death. While this change may not impact withdrawals from smaller inherited accounts, it will likely accelerate recognition of income for those inheriting much larger accounts. Assuming passage of the proposed legislation, owners of large retirement account balances will want to consider potential use of Roth IRA conversion strategies as part of their estate planning. Those individuals will also want to review current estate plans for provisions contained in any trusts designated as retirement account beneficiaries, to avoid potential unintended consequences resulting from the acceleration of distributions under the SECURE Act.

The above changes would not apply to accounts inherited by a beneficiary as a result of a death occurring on or before December 31, 2019. The ten-year rule would apply to a downstream beneficiaries of current owners of inherited IRA upon the death of the current owner after December 31, 2019.

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[1] Setting Every Community Up for Retirement Enhancement (SECURE) Act was passed by the U. S. House of Representatives on May 23, 2019. Similar legislation, known as the Retirement Enhancement and Savings Act (RESA), was considered by the Senate but never reconciled with the SECURE Act provisions.