

Tax and Retirement Planning: The SECURE Act in 2020

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The Setting Every Community Up for Retirement Enhancement Act (SECURE Act) recently became law. Many of the provisions go into effect in 2020, which means now is the time to review how these changes affect your tax and retirement planning.

This alert takes a look at some of the more salient provisions of the SECURE Act that apply to individuals. The changes might provide you and your family with tax-savings opportunities. Not all of the changes are favorable, however, and there may be steps you can take to minimize their impact.

Lifetime ability to contribute to traditional IRAs. Before 2020, traditional IRA contributions were not allowed after age 70½. Starting in 2020, an individual of any age can make contributions to traditional IRAs, as long as the individual has compensation, which generally means earned income from wages or self-employment.

Required minimum distribution age raised from 70½ to 72. Before 2020, retirement plan participants and IRA owners were generally required to begin taking required minimum distributions (RMDs) from their plan by April 1 of the year following the year they reached age 70½. For RMDs after Dec. 31, 2019, for individuals who attain age 70½ after that date, the age at which individuals must begin taking RMDs is increased from 70½ to 72.

Partial elimination of stretch IRAs. For deaths of plan participants or IRA owners occurring before 2020, beneficiaries were generally allowed to stretch out the tax-deferral advantages of the plan or IRA by taking distributions over the beneficiary's life or life expectancy (in the IRA context, this is sometimes referred to as a "stretch IRA"). However, for deaths of plan participants or IRA owners beginning in 2020, distributions to most non-spouse beneficiaries are generally required to be distributed within ten years following the plan participant's or IRA owner's death. So, for those beneficiaries, the "stretching" strategy is no longer allowed.

Exceptions to the 10-year rule are allowed for distributions to (1) the surviving spouse; (2) a child who has not reached majority; (3) a chronically ill individual; and (4) any other individual who is not more than ten years younger than the plan participant or IRA owner. Those beneficiaries who qualify may generally still take their distributions over their life expectancy.

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Expansion of Section 529 education savings plans to cover registered apprenticeships and distributions to repay certain student loans. A Section 529 education savings plan is a tax-exempt program established and maintained by a state, or one or more eligible educational institutions. Any person can make nondeductible cash contributions to a 529 plan on behalf of a designated beneficiary. The earnings on the contributions accumulate tax-free. Distributions from a 529 plan are excludable up to the amount of the designated beneficiary's qualified higher education expenses.

Before 2019, qualified higher education expenses didn't include the expenses of registered apprenticeships or student loan repayments. But for distributions made after Dec. 31, 2018 (the effective date is retroactive), tax-free distributions from 529 plans can be used to pay for fees, books, supplies, and equipment required for the designated beneficiary's participation in an apprenticeship program. In addition, tax-free distributions (up to \$10,000) are allowed to pay the principal or interest on a qualified education loan of the designated beneficiary, or a sibling of the designated beneficiary.

Retirement plan withdrawals for birth or adoption expenses. Generally, a distribution from a retirement plan must be included in income. And, unless an exception applies (for example, distributions in case of financial hardship), a distribution before the age of 59½ is subject to a 10% early withdrawal penalty on the amount includible in income.

Starting in 2020, plan distributions (up to \$5,000) that are used to pay for expenses related to the birth or adoption of a child are penalty-free. That \$5,000 amount applies on an individual basis, so for a married couple, each spouse may receive a penalty-free distribution up to \$5,000 for a qualified birth or adoption.