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Elder Law Guys: Congress has come for your money

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On Dec. 20, President Donald Trump signed into law the 47-page "Setting Every Community Up for Retirement Enhancement" Act.

The act, nicknamed the SECURE act, was three years in the making and was designed, supposedly, to provide additional retirement income security. It went into effect the first of this year.

The act — part of a $1.4 trillion spending bill — is estimated by the Congressional Research Service to generate approximately $16.4 billion in revenue over the next 10 years. Almost $15.7 billion will come from the elimination of the "stretch" option for individual retirement accounts.

Let's highlight some non-stretch changes first:

1. The required starting date for taking required minimum distributions — amounts that tax law requires be withdrawn annually from your IRA or 401(k) — has been extended from age 70½ to age 72. Looks like Congress finally noted that people are generally living and working longer.

Note also that the IRS is in the process of revising life expectancy tables, which determine the percentage amount for an required minimum distribution based upon your age.

2. Elimination of the age limit for traditional IRA contributions was approved. Previously 70½ was the age limit for those still working.

3. The act eliminates the 10% early withdrawal penalty for births or adoption, up to $5,000 for each birth or adoption. That amount is still subject to taxation, but not the penalty.

4. The qualified charitable distribution of up to $100,000 per year in a trustee-to-trustee transfer without having it as part of your taxable required minimum distribution remains at age 70½ instead of going to age 72.

Now, let's take a look at the act's provision that will affect most of our clients — especially their loved ones and even possibly you, dear reader: the Death of the Stretch IRA.

A quick summary is in order. Under the old rules, inherited individual retirement accounts and 401(k)s could be "stretched" out over the life expectancy of your beneficiary.

For most beneficiaries, the new act requires that the entire account be distributed within 10 years after the account owner dies. Why? Well, part of the rationale was that these accounts were for funding the account owner's retirement — not to provide a long-term legacy to beneficiaries.

Let's assume you turned 75 in 2019 and had $300,000 in your IRA at the end of 2018. Using the IRS age 75 divisor of 22.9, or roughly 4.37%, your required required minimum distribution for 2019 would be $13,100.

Let’s further assume — perish the thought — that you died in 2019 and named your son, age 44, as your beneficiary with the same $300,000 IRA account balance.

Your son, under the old rules, could then stretch out that over his own life expectancy (38.8 years or 2.8% of your 2018 balance) generating an annual required minimum distribution of roughly $7,730. Have a little fun by changing the IRA amounts and non-spouse beneficiary ages and see what a dramatic result can be.

Now, it’s 2020. If instead of dying last year, you die this year, things change. Your now 46-year-old beneficiary son would have to liquidate this account by the end of the 10th year (age 56) and could not stretch it over his projected life expectancy of 84 years or another 38 years.

As we are somewhat limited in space for this column, we can’t get into the many nuances of the act. However, we’d like to point up some rather important portions.

Congress created a group of beneficiaries who are not subject to the new 10-year rule. These include:

1. A surviving spouse.

2. A minor child who has not yet attained majority status (but, not grandchildren. Once majority is attained, they would be subject to the 10-year rule).

3. An individual who is disabled, under the official rules.

4. A chronically ill individual, again that meets the official definition of that.

5. An individual who is not more than 10 years younger than the IRA owner.

Now, the real problem for many people will be those who created a “conduit” or “pass through” trust for beneficiaries in which the trust had mandated that individual for whatever reason (they are spendthrifts, in a bad marriage, could not otherwise be trusted, etc.), would receive on the required minimum distribution.

What’s the upshot of all of this?

The rules for retirement planning and inheritance are certainly changing as a result of the SECURE Act. Our best advice: Review your personal situation, your IRA balance, your beneficiaries (your and their tax situations) and what you now want to do.

Options could include taking out more than your required minimum distributions; buying life insurance that benefits those who had been slated to receive your IRA account proceeds (it’s tax free); or establishing a charitable remainder trust. Then, sit down with your trusted advisors to determine how best to proceed. And do it quickly!

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