The SECURE Act

Highlights, Planning Opportunities, and Challenges

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Say hello to Today's speakers

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Dana Vosburgh, CFP	**Veronica Van Nest, JD**	**Margaret Jeffries, CFP**
Managing Director Advisory Services	Wealth Management Senior Consultant	Wealth Management Consultant

The SECURE Act

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What is it?

- Setting Every Community Up for Retirement Enhancement (SECURE) Act
- Designed to expand and preserve retirement saving options for more Americans with 29 new provisions or major changes
- Affects both individuals and business owners
- Passed by the U.S. House of Representatives in May 2019, then by the Senate as part of the December 19, 2019 spending bill
- Signed into law by President Trump on December 20, 2019

Highlights

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For Individuals:

- Repeals IRA contributions age limit
- Increases Required Minimum Distribution (RMD) age to 72
- Elimination of 'Stretch' IRA
- Expands 529 Plan capabilities and qualifying education costs
- Penalty-free withdrawals for births and adoptions
- Kiddie Tax reverted to pre-Tax Cuts and Jobs Act (TCJA) tax rates

IRA Contributions Allowed after 70 ½

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Under current law, Traditional IRAs are the only retirement account for which contributions are not permitted for working individuals after a certain age (70 ½)

Individuals of any age will now be allowed to contribute to a Traditional IRA. Such individuals must have earned income from either wages or self-employment

Working individuals must still begin RMDs from Traditional IRAs at age 72 even if still contributing

Planning Opportunity: As life expectancies continue to rise and the ability to now contribute to an IRA regardless of age, consider a part-time job or hobby that can provide earned income. If a spouse is still working, consider taking advantage of the spousal IRA rules

Required Minimum Distributions (RMDs)

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Increases the mandatory age individuals must begin taking RMDs from 70 ½ to 72 years old

Eliminates the idea of 'half-birthdays', simplifying in what year RMDs are to begin

This change only applies to individuals who turn 70 ½ on or after January 1, 2020. Those who turned 70 ½ by the end of 2019 will still take RMDs in 2020 and thereafter under existing rules, even if younger than age 72

Age of IRA holder:	First RMD Must Be Taken By:
Turn 70 in 2019 before July 1	April 1, 2020*
Turn 70 in 2019 on or after July 1	April 1, 2022
Turn 70 in 2020 (turn 72 in 2022)	April 1, 2023

*The subsequent RMD (i.e., for 2020) must also be taken by December 31st, 2020

Elimination of the "Stretch" IRA

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The Act requires most beneficiaries of any IRA owners that pass away on or after January 1, 2020 to withdraw the entire Inherited IRA balance by no later than the 10th full year following the IRA owner's death, therefore eliminating the popular 'stretch' IRA strategy for most beneficiaries

Under the new 10-year rule there is no annual required minimum distribution, the entire inherited IRA must simply be emptied by the end of the 10th year following the year of inheritance

The new 10-year rule does not apply to "Eligible Designated Beneficiaries", who can elect the 10-year rule OR take RMDs over their lifetimes under previous "Stretch" IRA rules. These include:

- spousal beneficiaries,
- disabled,
- chronically ill,
- individuals who are not more than 10 years younger than the decedent, and
- certain minor children (son or daughter of the original account owner), but only until they reach the age of majority, at which time the 10-year window begins

Existing Inherited IRAs (i.e., IRAs whose owners passed away on or before December 31st, 2019) are grandfathered in under the previous RMD rules. Designated beneficiaries (individuals and certain qualifying trusts) remain eligible to stretch distributions over their life expectancy or, in the case of a qualifying trust, over the oldest beneficiary's life expectancy

Elimination of the "Stretch" IRA Cont'd

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Planning Opportunity: The new '10-year Rule' still allows some flexibility in the timing of distributions for beneficiaries

Example: On September 1st, 2020, Tom, age 78, passes away and leaves equal shares of his $1,000,000 IRA to his two nephews, Jack who is 45 and Frank who is 50 years old and are not disabled or chronically ill

To avoid being penalized, Jack and Frank must each withdraw their $500,000 Inherited IRA balances by no later than the end of the 10th full year following Tom's death (i.e., December 31st, 2030)

Prior to December 31st, 2030, Jack has limited income of his own and decides to use his Inherited IRA to supplement his spending needs. He withdraws $30,000 at the beginning of each year and then withdraws the remaining balance of $200,000 on December 31st, 2030

Frank has more than enough income to meet his spending needs and decides to delay taking withdrawals for as long as possible. As a result, he does not take any withdrawals until the December 31st, 2030 deadline when he withdraws the entire $500,000

Expands 529 Plan Qualified Education Expenses

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Registered apprenticeship programs and trade schools and the costs associated with the programs (e.g., registration fees, books, supplies, and equipment) are now included under the definition of eligible post-secondary institution expenses that can be paid Federal income tax and penalty free from 529 Plans

In addition, qualified student loans can be paid off using 529 Plan funds Federal income tax and penalty free, limited to a lifetime amount of $10,000 per person (beneficiary). Additional distributions of $10,000 for each of the beneficiary's sibling's outstanding student debt is also permitted

Effective for distributions made after December 31, 2018

It is important to note that this change was made at the Federal level and that, similar to when the Federal definition of qualifying expenses was expanded to include K – 12 tuition expenses of up to $10,000 starting in 2018, each State will rule separately on whether to follow the SECURE Act's lead and allow these distributions income tax and penalty free at the state level

Penalty-free Withdrawals for Births and Adoptions

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Section 113 of the Act creates a new exception to the 10% penalty on early withdrawals for 'Qualified Births or Adoption Distributions', although distributions are still subject to income tax like any other tax-deferred retirement account

A 'Qualified Births or Adoption Distribution' of up to $5,000 per retirement account owner is allowed within one year following when the birth has occurred or adoption is finalized, in other words, after the 'qualifying event' has occurred

If both parents maintain retirement assets, they can each take a distribution up to the $5,000 limit (i.e., up to $10,000 per couple) for each new birth or adoption

Kiddie Tax Reverts to Pre-TCJA Tax Rates

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A "Kiddie Tax" is imposed on unearned income of dependent children under the age of 18, or age 23 if a student, over their deduction amount

Prior to 2018, unearned income was taxed at their parent's marginal tax rate

The TCJA was scheduled to increase the "Kiddie Tax" on unearned income in 2018 - 2025 over a certain threshold (i.e., over $2,100 in 2018 and $2,200 in 2019) taxing it at the highest income and capital gains tax rates for Estate and Trusts

Section 501 of the Act repealed this provision and the parent's marginal tax rate will be used again effective as of tax year 2020. Further clarification is expected regarding retroactively applying the rates to unearned income in tax years 2018 & 2019.

Unearned income in 2018 over $12,500 was taxed at 37% and once income reached $12,950 any capital gains were to be taxed at 20%. The 3.8% Medicare contribution tax was also imposed on income over $12,950

Planning Opportunity: Individuals that had a meaningful amount of unearned income in 2018 should review their 2018 tax return with their CPAs and, if beneficial, can apply for a refund for the difference in taxes due.

What Hasn't Changed?

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The SECURE Act did not change when Social Security benefits can be taken (i.e., reduced benefits as early as age 62, full benefits at Full Retirement Age of 66 or 67, or increased benefits if delayed until as late as age 70)

Qualified Charitable Distributions (QCDs) of up to $100,000 per year from IRAs made directly to qualifying charities are still allowed beginning at age 70 ½, even if required minimum distributions do not begin until age 72

The IRS life expectancy tables used to calculate required minimum distributions for IRA owners and beneficiaries remain unchanged as of 2020. However, the IRS has proposed to update each of the tables to reflect that individuals are living longer and as a result RMDs should be slightly lower at each age. The new factors are expected to go into effect beginning in 2021 or 2022

Planning Opportunity: Use QCDs, beginning after age 70 ½, to satisfy the giving 'itch' and to reduce Traditional IRA balances and therefore future RMDs beginning at age 72

Provisions for Business Owners to Encourage 401(k) Participation

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- Easing of rules for annuities in 401(k)s
- Employers with safe harbor 401(k) plans using "auto-enrollment" and automatic escalation can raise their cap from 10% to 15% of compensation for eligible participants after the first year
- Increases tax credits for small business
- Relaxes rules for multi-employer plans
- Allows part-time workers ability to participate in plans
- Eliminates some safe harbor notice requirements

Lifetime Income Options (Annuity Contracts) in 401(k)s

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Creates a 'safe harbor' for plan administrators (fiduciaries) to include annuities in 401k plans as an 'investment' option

Requires retirement plan statements to include a lifetime income disclosure at least once during any 12-month period

The Act also creates a new 'distributable event' for current or former employees that applies just to annuities that are being removed as an option of a plan.

Increased Small Business Tax Credits

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Applicable for employers with 100 or fewer employees

Increases qualified retirement plan startup costs credit - Increases the current $500 tax credit cap (for the plan's first three years) to the greater of (1) $500 or (2) the lesser of (a) $5,000 or (b) $250 multiplied by the number of non-highly compensated employees eligible to participate in the plan

Automatic enrollment credit - Small employers that adopt automatic enrollment provisions are eligible for an additional $500 credit for three years regardless of when the automatic enrollment provisions are adopted. Automatic enrollment places new employees in retirement plans automatically so that they have to opt-out rather than opt-in

Both credits are available beginning in tax year 2020

MEPs and PEPs

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The Act has given us PEPs (Pooled Employer Plans), a newer, more open version of MEPs (Multiple Employer Plans).

MEPs (or PEPs) are retirement plans (either defined-benefit or defined-contribution) adopted by two or more unrelated employers resulting in lower costs and simplified administration

The Act relaxes the rules for unrelated small businesses and employers to band together and participate in MEPs (or PEPs)

- Employers are no longer required to have common businesses, reside in the same geographic location, or have a significant relationship
- Mitigates the 'One Bad Apple' rule, whereby a disqualifying act by any single actor would disqualify the entire plan

Expanded Participation for Part-Time Workers

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Currently, part-time workers who work at least 1,000 hours in one year are allowed to participate in their workplace retirement plan

Beginning in 2021, the Act expands this right to workers with at least 500 hours of work in three consecutive 12-month periods, meaning employees will not be eligible until 2024

These new participants can be excluded from top-heavy requirements, nondiscrimination and safe harbor contributions

Questions?

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