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PCS CLIENT ALERT: THE SECURE ACT

The end of the decade brought with it drastic changes to retirement benefits, some of which may affect your estate planning.

The SECURE Act (officially named the Setting Every Community Up for Retirement Enhancement Act of 2019) was signed into law on December 20, 2019. This Act increases access to tax-advantaged retirement accounts and eases compliance burdens for plan sponsors. On the estate planning side, this Act severely limits the ability to “stretch” the tax deferral benefit of inherited retirement accounts. This Alert provides a brief summary of the Act.

PARTIAL ELIMINATION OF THE IRA STRETCH

Under prior law, IRAs and other qualified plans that were left to a non-spouse individual, such as a child or grandchild, could be withdrawn annually over the course of that beneficiary's life expectancy, resulting in favorable income tax deferral. The SECURE Act removes that benefit by requiring that most retirement assets inherited in 2020 and beyond be distributed within a 10-year period, effectively accelerating the depletion of inherited accounts.

Note that this 10-year distribution period does not apply to “eligible designated beneficiaries,” defined as (i) the surviving spouse, (ii) a minor child of the plan participant (though the 10-year period will commence when that child reaches the age of majority), (iii) a disabled beneficiary, (iv) a chronically ill beneficiary, or (v) a beneficiary who is less than ten

years younger than the plan participant.

The SECURE Act is a major change in the law and creates the need for you to review your estate plan and beneficiary designations with your Wiggin and Dana attorney. The limited stretch for your beneficiaries may create an income tax burden much sooner than anticipated. Additionally, if retirement plans pass through your estate plan into a trust for your beneficiaries, those trusts should be reviewed to determine (a) if the trusts will qualify for the 10-year distribution period and (b) if the retirement accounts and the new rules change the underlying structure of your plan (such as age distribution trusts for children or grandchildren, asset protection trusts, or equalization clauses among beneficiaries). Additionally, there may be planning opportunities available to offset the loss of the income tax deferral, including the use of charitable trusts or life insurance. We look forward to reviewing your plan with you to review the impact of this new law.

Although the loss of the stretch feature will be seen as a negative change for many clients (or their beneficiaries), the SECURE Act includes several provisions designed to boost the usefulness of retirement plans for the individual saving for retirement.

INCREASED AGE FOR REQUIRED MINIMUM DISTRIBUTIONS

Prior law required retirement account owners to begin taking “required minimum

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distributions" ("RMDs") at age 70½. But for those account owners who are not 70½ by the end of 2019, that beginning date is extended to age 72. By delaying the initiation of RMDs, you can allow time for additional asset growth, as well as an additional deferral of income recognition.

NO AGE LIMITATION ON IRA CONTRIBUTIONS

Prior to the SECURE Act, an individual over the age of 70½ could not contribute to an IRA. The Act has eliminated this restriction and repealed the age cap for traditional IRA contributions.

INCREASED ACCESS TO RETIREMENT PLANS FOR SMALL BUSINESS OWNERS AND PART-TIME EMPLOYEES

The Act will make it simpler for small business owners to set up and offer 401(k) plans. Small companies can band together to open 401(k) multiple-employer plans (MEPs) (also referred to as pooled employer plans (PEPs)), reducing cost and administrative burdens. MEPs are currently permissible, but only for related businesses, such as businesses with a common owner; the SECURE Act has eliminated this nexus requirement.

Prior to the SECURE Act, employees who did not work at least 1,000 hours during the calendar year were not eligible to participate in their employer's defined contribution plan. The Act will provide access for eligible part-time and temporary employees who have worked at least 500 hours per year for at least three consecutive years to participate in employer-sponsored retirement plans.

INCREASED ANNUITY OPTIONS

Prior to the SECURE Act, annuities were offered in less than 10% of 401(k) plans, largely due to liability concerns about

annuity providers. The Act seeks to remedy this by including a provision that provides a fiduciary safe harbor to 401(k) plan sponsors who include annuities among offerings to plan participants.

ANNUAL LIFETIME INCOME DISCLOSURE STATEMENTS

In order to gain a better understanding of what your monthly income might be when you retire, the SECURE Act requires 401(k) plan administrators to provide annual lifetime income disclosure statements to plan participants. These statements will show how much income the lump sum balance in the retirement account could yield.

The disclosure statements will not be released until one year after the IRS issues interim final rules, creates a model disclosure statement and releases assumptions that plan administrators can use to convert account balances into annuity equivalents.

PENALTY-FREE WITHDRAWALS FOR THE BIRTH OF A CHILD OR AN ADOPTION

Under the SECURE Act, an owner of a 401(k), IRA or other retirement account may withdraw up to \$5,000 following a qualified birth or adoption of a child without paying the 10% early-withdrawal penalty tax. The distribution must occur within one year of the child being born or the adoption being finalized. Note that if you are married, each spouse can withdraw \$5,000 from his or her own retirement account without penalty.

If you have any questions about how the SECURE Act may impact your estate plan, or specifically, your retirement benefits, please contact your Wiggin and Dana attorney.