



How does the SECURE Act affect your Estate Plan?

By Nicholas Crivella, Esquire and Brittney Grizzanti, Esquire

EXECUTIVE SUMMARY

Congress recently enacted legislation that will expedite Required Minimum Distributions that must be paid from inherited retirement accounts which will accelerate income tax liability. Additionally, if inherited retirement accounts are payable to a trust for the benefit of a beneficiary, this new legislation can cause unplanned outright distributions of trust assets to such beneficiaries. Please read below for a more detailed explanation of how your estate plan may be impacted.

DETAILED EXPLANATION

In December 2019, Congress passed the Setting Every Community Up for Retirement Enhancement Act ("SECURE Act"). This new legislation made several key changes to how retirement accounts can be distributed to an account owner's beneficiaries upon their passing. The most significant change relates to Required Minimum Distributions.

Traditional retirement accounts (IRAs, 401(k)s, etc.) are funded with pre-tax dollars, allowed to grow tax free and subject to income tax only upon withdrawal. The longer you are able to defer withdrawing assets from a traditional retirement account, the longer you can defer the income tax liability. Traditionally, the deferral of income was allowed until age 70 ½, at which time the account owner was required to start taking mandatory withdrawals from the account, creating an income tax liability on the withdrawn funds ("Requirement Minimum Distributions" or "RMDs"). **Under the new SECURE Act, the required start date for RMDs has been extended from 70 ½ to 72 years of age.**

RMDs are relevant in estate planning as clients name individual beneficiaries (i.e. family and/or friends) to receive their retirement accounts upon their passing. Generally, upon passing a named beneficiary will receive the account as an Inherited IRA.

Prior to the SECURE Act, most beneficiaries of an Inherited IRA were required to immediately begin taking RMDs out of the account and begin paying income tax. The amount to be withdrawn was based on the beneficiary's life expectancy, which could significantly delay income tax recognition, especially for younger beneficiaries ("Stretch"). **With minor exceptions, the ability for most beneficiaries to Stretch RMDs**



from an Inherited IRA based on their life expectancy was taken away under the SECURE Act in favor of a mandatory 10-year term to withdraw all assets from the retirement account.

For clients with a desire to distribute assets to their beneficiaries outright, the new SECURE Act means that the beneficiary will need to pay income tax on any Inherited IRA sooner than they would have prior to the SECURE Act (within 10 years of the original account owner's date of death). **Although this will create a greater income tax liability earlier, if your plan is to distribute retirement accounts outright, then there is likely no change needed to your estate planning documents.** Clients are encouraged to seek advice from their financial and accounting professionals related to additional planning alternatives to reduce the burden of this expedited income tax liability (including the potential conversion of traditional retirement accounts to Roth accounts).

Alternatively, many of our estate planning clients choose to retain assets in trust for a beneficiary as opposed to giving an outright distribution (i.e. for a minor beneficiary, for estate tax purposes, for spendthrift concerns, creditor protection, etc.). Prior to the SECURE Act, in order to maintain the benefit of a Stretch for a retirement account payable to a trust, the trust agreement had to be drafted as a "Conduit Trust". When a Conduit Trust is the beneficiary of a retirement account, it requires the payment of all RMDs to be paid immediately to the individual beneficiary, outright. This outright payment of RMDs allowed the IRA to "look through" the trust and use the life expectancy of the individual beneficiary in determining the RMDs, thus ensuring the ability to Stretch the Inherited IRA over their lifetime.

However, now with the ability to Stretch taken away for most beneficiaries in favor of a 10-year payout requirement, this means that all retirement assets held within a Conduit Trust will be distributed outright to a trust beneficiary within 10 years of the client's death. For these client's with trusts named as beneficiaries of their traditional retirement accounts, the SECURE Act may require a review and possible update to your estate planning documents. Specifically, client's may choose to revise their planning to remove the Conduit Trust language in favor of a trust that accumulates all RMDs and distributes pursuant to trustee discretion ("Accumulation Trust").

Unfortunately, the Accumulation Trust is not without its downside. Specifically, any retained RMDs not paid outright to a beneficiary will be taxed at trust income rates which are typically much higher than a beneficiary's individual rates (i.e. 37% on all income over \$12,750). The shift in planning from a Conduit Trust to an Accumulation Trust will not defer or reduce income tax liability on retirement accounts. It will, however, ensure that all IRA proceeds remain in trust as opposed to being distributed outright to a trust beneficiary before otherwise intended.



Please note, under the SECURE Act certain categories of beneficiaries ("Eligible Designated Beneficiaries") are still allowed to Stretch their RMDs. These categories include:

- (i) A **surviving spouse** can continue to rollover the IRA to their own IRA or Stretch the Inherited IRA over their life expectancy.
- (ii) An **account owner's minor child** can Stretch based on their life expectancy until they reach age of majority (or up to 26 if still in school) with a 10-year payout thereafter (please note this exception only counts if the minor is the specific account owner's child).
- (iii) A beneficiary who is **disabled** or **chronically ill** can Stretch over their life expectancy.
- (iv) A beneficiary who is **not more than 10 years** younger than the account owner can Stretch over their life expectancy.
- (v) A beneficiary who has **received an Inherited IRA prior to December 31, 2019**.

For these Eligible Designated Beneficiaries, the use of a Conduit Trust in your estate planning still likely remains appropriate.

As with all estate planning, there is no one-size fits all solution. We are committed to helping our clients work through the impact of this new law. If you would like to schedule a one-on-one review of your estate planning documents to discuss the potential impact of the SECURE Act, please contact our office to coordinate a time to speak and/or meet with one of our attorneys. Depending upon demand, our firm may conduct a seminar on this topic. If you would be interested in attending any future seminar tailored to the SECURE Act please email bagley@bagleyrhody.com.

* The above is not legal advice and a personalized review is necessary to determine the exact impact of the SECURE Act on your planning.