ED SLOTT'S IRA ADVISOR

February 2020

Tax & Estate Planning For Your Retirement Savings

WHAT'S INSIDE?

SECURE Act: Ch-Ch-Ch-Ch-Changes! *Turn and Face the Strange*

- RMD Age Raised to 72
- Age Limit Eliminated for Traditional IRA Contributions
- Stretch Eliminated for *Most* Beneficiaries
- Creation of a New Class of Beneficiaries
- Successor Beneficiaries and the 10-Year Rule
- Stretch Eliminated for *Most* Trusts
- Discretionary (Accumulation) Trusts Will Work Better *...But at What Cost?*
- 10% Penalty Exception for Birth or Adoption
- SECURE Act Odds and Ends
- Planning Opportunities

<Pages 1-6>

Executive Summary

<Page 2>

Insert: Retirement Plan Payouts to Beneficiaries Under the SECURE Act

Guest IRA Expert
Natalie Choate, J.D.
Nutter McClennen & Fish LLP
Boston, MA

The SECURE Act's Unanswerable Questions

<Pages 6-8>

Join the Retirement Planning Conversation

SECURE Act: Ch-Ch-Ch-Ch-Changes!
Turn and Face the Strange

Following David Bowie's lyrical advice, we turn the calendar and face a strange new retirement world. The Setting Every Community Up for Retirement Enhancement (SECURE) Act was attached to this year's spending bill and signed into law on December 20, 2019 with the bulk of its provisions becoming effective on January 1, 2020. The tentacles of this new law are far reaching and will significantly impact millions of retirement account owners and their beneficiaries.

While some long-standing estate planning practices have been eliminated, new twists within the SECURE Act have opened savings doors to many who were previously shut out. Here is a detailed analysis of the changes that will have the most widespread effects.

RMD Age Raised to 72

The SECURE Act raises the age for beginning required minimum distributions (RMDs) to 72 for all retirement accounts subject to RMDs. Any IRA owner who turned 70½ in 2019 or earlier is still bound by the old rules and cannot take advantage of the new age 72 rule.

IRA owners reaching age 70½ in 2020 or later (those born on or after July 1, 1949) fall under the SECURE Act and will not have to take their first RMD until age 72. As with previous guidelines, the first RMD can be delayed until April 1 of the year after the account owner reaches age 72.

Example: Robert and Melinda are married. Robert's 70th birthday was June 30, 2019, and Melinda turned 70 the very next day, on July 1, 2019. This means Robert turned 70½ on December 30, 2019, and Melinda turned 70½ on January 1, 2020. While the couple is only separated in age by one day, their RMD required beginning dates are two years apart!

Since Robert turned 70½ in 2019, he is bound by the 2019 RMD rules. His first RMD is for 2019, which he can opt to delay until April 1, 2020. He gets no benefit from the SECURE Act, and he cannot skip a year until he is 72.

Melinda, on the other hand, benefits from turning 70½ in 2020. She follows the new RMD rules and is not required to take an RMD until the year she reaches age 72, which is 2021. She can delay her first RMD until April 1, 2022.

Age Limit Eliminated for Traditional IRA Contributions

The SECURE Act eliminated the 70½ age limit for traditional IRA contributions. Now, those who are still working can contribute to a traditional

ONLY A FEW SPOTS LEFT
Ed Slott and Company's Exclusive 2-Day IRA Workshop
INSTANT IRA SUCCESS
February 21-22, 2020 | San Francisco, CA
$400 OFF
Promo Code: NEWSLETTER

© 2020 Smart Subscriptions, LLC

Executive Summary

SECURE Act: Ch-Ch-Ch-Ch-Changes! *Turn and Face the Strange*

- The Setting Every Community Up for Retirement Enhancement (SECURE) Act was signed into law on December 20, 2019 with the bulk of its provisions becoming effective on January 1, 2020.
- The SECURE Act raises the age for beginning required minimum distributions (RMDs) to 72 for all retirement accounts subject to RMDs; any IRA owner who turned 70½ in 2019 or earlier is still bound by the old rules and cannot take advantage of the new age 72 rule.
- The SECURE Act eliminated the 70½ age limit for traditional IRA contributions.
- The lifetime stretch IRA is replaced with a 10-year rule for the vast majority of beneficiaries for deaths after December 31, 2019.
- The SECURE Act created five classes of "eligible designated beneficiaries" (EDBs) who are exempt from the IRA 10-year payout rule and can still stretch RMDs over their life expectancy.
- If the first beneficiary died before 2020, the successor does get to continue the stretch over the original beneficiary's remaining life expectancy; if an IRA owner dies after 2019, successor beneficiaries are automatically bound by the 10-year payout term.
- The SECURE Act eliminated the lifetime RMD stretch for the majority of trusts named as IRA beneficiaries and, in many cases, the 10-year payout will now apply.
- The SECURE Act created a new exception to the 10% early distribution penalty for "qualified birth or adoption distributions," which applies to both IRA and company savings plan distributions.
- While the age for RMDs was raised to 72 by the SECURE Act, qualified charitable distributions (QCDs) are still permitted at age 70½.
- The SECURE Act provides new liability protection for plan sponsors who wish to offer annuities in a company savings plan.

The SECURE Act's Unanswerable Questions

- Until further guidance, regulations or technical corrections are published, the answers to many SECURE Act questions are literally unknowable.
- The SECURE Act addresses estate planning for IRA owners and qualified plan participants by putting beneficiaries into three categories: eligible designated beneficiaries, non-designated beneficiaries, and designated beneficiaries.
- One major blind spot of the SECURE Act is its apparent ignoring of the possibility that IRA trusts might have multiple designated beneficiaries.

IRA, regardless of age. This new rule will create some confusion when combined with RMD requirements.

Example: Serena, age 75, is self-employed. Despite having earned income for the past few years, Serena has not been allowed to contribute to her IRA due to the 70½ age restriction. She has diligently taken her RMDs. (There is no "still-working exception" for IRAs.) With the new rules eliminating the age restriction on traditional IRA contributions, Serena can now contribute. However, she must also continue taking her RMD.

This "in-and-out" of contributions and RMDs will become commonplace. Keep in mind there is no age restriction on Roth IRA contributions. Also, the elimination of the age restriction on traditional IRAs may open a Backdoor Roth opportunity to those over age 70½ with income over the Roth contribution limits.

Stretch Eliminated for *Most* Beneficiaries

The lifetime stretch IRA is replaced with a 10-year rule for the vast majority of beneficiaries. Generally, this change applies to deaths after December 31, 2019.

However, the effective date is extended for two years (for deaths after December 31, 2021) for governmental plans, including 403(b) and 457(b) plans and the Thrift Savings Plan. It is also extended for as long as two years for collectively bargained plans, depending on the expiration date of the union contract. ***(Note that the new rules do not apply to defined benefit plans.)***

The 10-year rule dictates that accounts must be emptied by December 31 of the tenth year following the year of death. There will be no annual RMDs.

Instead, the only RMD on inherited IRAs (including Roth IRAs) is the balance at the end of the 10 years after death. For deaths in 2019 or earlier, regardless of whether the beneficiary has claimed the account yet, the old stretch rules are grandfathered.

> The only RMD on inherited IRAs (including Roth IRAs) is the balance at the end of the 10 years after death.

Example: Thomas, age 32, inherits a Roth IRA from his father who died in 2020. Thomas is subject to the new 10-year rule. Thomas can take as much or as little out of the inherited Roth IRA each year during the 10-year period, but he must withdraw the entire Roth IRA by December 31, 2030. Any amount that remains in the account after that date will be subject to the 50% missed RMD penalty.

Had Thomas' father passed away in 2019, Tom would have been entitled to stretch the inherited Roth IRA based on pre-SECURE Act guidelines.

Creation of a New Class of Beneficiaries

The stretch IRA is not a thing of the past for all beneficiaries. The SECURE Act created five classes of "eligible designated beneficiaries" (EDBs) who are exempt from the 10-year payout rule and can still stretch RMDs over their life expectancy.

This new group of eligible designated beneficiaries includes:

1. Surviving spouses;
2. Minor children of the account owner until age of majority – *but not grandchildren;*
3. Disabled individuals;
4. Chronically ill persons; *and*
5. Beneficiaries not more than ten years younger than the IRA owner.

Under the SECURE Act, each of these newly created classes of EDBs has its own rules. Minors are determined based on state law (usually age 18 is the age of majority) but could still be considered a "minor" up to age 26 if still in school.

"Disabled" uses the restrictive definition from Tax Code §72(m)(7), which requires the individual to be unable to perform any job because of a "physical or mental impairment" expected to result in death or continue indefinitely.

A "chronically ill" individual is based on the definition under Tax Code §7702B(c)(2) for long-term care insurance purposes. To qualify as "chronically ill," the person would have to be certified by a licensed health care practitioner to be unable to perform at least two activities of daily living for at least 90 days or require "substantial supervision" due to a severe "cognitive impairment."

Example [of an EDB minor]: In 2020, Madaleine, age 10, inherits an IRA from her mother. Madaleine is an eligible designated beneficiary and can stretch distributions over her single life expectancy. This goes on for 8 years. Madaleine's 18th birthday is in 2028 and she is no longer in school.

Because Madaleine has reached the age of majority, the 10-year rule will then apply. Madaleine must empty the inherited IRA by December 31, 2038 — *by the end of the 10th year after reaching the age of majority (which in her state is age 18).*

Example [of an EDB not more than 10 years younger than the original account owner]: Three sisters Eldest, Middle and Youngest are ages 70, 61 and 59, respectively. Eldest dies in 2020 and leaves an IRA to each of her siblings.

Since Middle (age 61) is less than 10 years younger than Eldest, she qualifies as an eligible designated beneficiary and can stretch RMD payments over her single life expectancy (20+ years).

Youngest is only age 59. She is more than 10 years younger than Eldest. Therefore, she is not considered an EDB and is bound by the 10-year payout term.

The timing of when a person is determined to be an EDB is also important. From the Act:

> *"Time for Determination of Eligible Designated Beneficiary - The determination of whether a designated beneficiary is an eligible designated beneficiary shall be made as of the date of death of the employee."*

Example [of a non-eligible designated beneficiary becoming an EDB too late]: Dad dies in 2020. He named Son, age 30, as his primary beneficiary. Son is bound by the SECURE Act which dictates he must use the 10-year payout for the inherited IRA.

Son gets into a car accident 6 months later and before Dad's IRA was titled in his name as an inherited IRA. Son is now fully disabled under the tax code rules. Son still cannot stretch the inherited IRA over his life expectancy. He cannot qualify as an EDB for his father's IRA, because he was not disabled as of the date of Dad's death.

Successor Beneficiaries and the 10-Year Rule

If an IRA owner dies after 2019, successor beneficiaries (beneficiaries of the original beneficiary) are subject to the 10-year rule. If an owner dies before 2020 and the original beneficiary dies after 2019, the

successor must always use the 10-year rule. However, if the original beneficiary also died before 2020, the successor does get to continue the stretch over the original beneficiary's remaining life expectancy.

Example [When original IRA owner died in 2019 and first beneficiary dies in 2020]: Grandma Carla dies in 2019. She named Daughter Ann, age 48, as her primary beneficiary. Even though Daughter Ann is not an EDB under the SECURE Act, she gets to stretch RMD payments because Grandma Carla died in 2019.

Daughter Ann dies in 2020 with Grandson Paul (age 12) as her successor beneficiary. Grandson Paul is subject to the 10-year rule and must receive the remaining funds in the inherited IRA by the end of the 10th year following Daughter Ann's death.

Had Daughter Ann also died in 2019, then the old rules would have applied, and Grandson Paul could have continued the stretch. Successor beneficiary rules are based on the year of death of the original beneficiary.

Stretch Eliminated for *Most* Trusts

The SECURE Act eliminated the lifetime RMD stretch for the majority of trusts named as IRA beneficiaries. In many cases, the 10-year payout will now apply.

Since most trusts were established for post-death control, it is essential that existing trusts be reviewed for all trust beneficiaries to receive the most favorable distribution options. Most trusts will have to be revised or completely redone.

Example: Grandpa Oscar set up a trust for his spendthrift grandson, Jake, age 30. The trust is a conduit trust with language carefully crafted saying each RMD must be paid out from the inherited IRA and then distributed to Jake. Grandpa Oscar intended to have RMDs stretched out over Jake's lifetime to keep him from quickly burning through the entire account.

Grandpa Oscar dies in 2020 without revising the trust. In the wake of the SECURE Act, the trust will no longer work as planned. There will be no annual RMDs. Instead, the 10-year rule will apply. The entire IRA balance will be distributed to the trust and then to spendthrift Jake in 2030. This nullifies any further trust protection and is exactly the opposite of what Grandpa Oscar wanted.

The SECURE Act does include provisions allowing trusts for the disabled or chronically ill to stretch RMDs from an inherited IRA over the life expectancy of the trust beneficiary — *even if such trusts have other designated beneficiaries who are not EDBs.* Those trust beneficiaries who are not disabled or chronically ill would be subject to the 10-year payout rule.

However, not everything in the SECURE Act is crystal clear. Further guidance is needed as to whether such treatment would be available for trusts with both non-EDBs and other EDBs besides disabled or chronically ill individuals (such as a spouse or a minor child).

Example: Barbara is an IRA owner who names her trust as IRA beneficiary. The trust beneficiaries are her minor child, Jessica, and her older child, Walter.

When Barbara dies, would both Walter (a non-EDB) and Jessica (an EDB minor) be stuck with having their IRA shares paid within 10 years of Barbara's death? Or, could minor Jessica stretch out RMDs until she reaches the age of majority and then have her remaining share paid out within 10 years? The SECURE Act is unclear.

The SECURE Act eliminated the lifetime RMD stretch for the majority of trusts named as IRA beneficiaries.

Discretionary (Accumulation) Trusts Will Work Better *...But at What Cost?*

If a trust is still deemed necessary, then a discretionary trust would work since inherited IRA funds can still be retained and protected in the trust, even after the 10 years. But all of those funds will still be taxed either at extremely high trust tax rates for dollars retained in the trust or at the beneficiaries' personal tax rates for distributions paid out of the trust.

While a discretionary trust provides the protection clients desire, it will come at a potentially prohibitive tax cost. As such, this may not be an acceptable alternative.

Example: Patricia knows her adult children are not responsible with money, so she named a discretionary trust as beneficiary of her IRA. Patricia dies in 2020. The trust is subject to the 10-year rule, but the trustee can spread payouts to the trust and Patricia's children over the ten years.

However, any funds remaining in the inherited IRA must be paid into the trust by December 31, 2030 (ten years after Patricia's death). Taxes must either be paid by Patricia's children if the funds are distributed to them or by the trust at high tax rates if the funds remain in the trust for continued protection.

10% Penalty Exception for Birth or Adoption

The SECURE Act created a new exception to the 10% early distribution penalty for "qualified birth or adoption distributions." The exception applies to both

IRA and company savings plan distributions.

A distribution is qualified if it is made from an IRA or company plan within one year of the date of birth or the date on which the adoption is finalized. There is a $5,000 lifetime (not annual) limit per birth or adoption on penalty-free withdrawals. The exception applies only to distributions made after the adoption of a child younger than age 18 or physically or mentally incapable of self-support. Although a qualified distribution may be penalty-free, it is still subject to tax.

There is a $5,000 lifetime (not annual) limit per birth or adoption on penalty-free withdrawals.

A married couple can each take $5,000 per child. There is no requirement that the distributions be used for birth or adoption expenses, and the distributions can be repaid all or in part at any time in the future.

Withdrawals from a company plan can be repaid back to the same company plan (but only if the employee is still eligible to participate in the plan) or to an IRA. Withdrawals from an IRA can only be repaid to an IRA – *not to a company plan.* Any repayments will be treated as a direct trustee-to-trustee transfer, and repayments to a company plan will be treated as an eligible rollover distribution.

The SECURE Act does not specify the tax treatment of qualified birth or adoption distributions that are repaid. Since the taxpayer has already been taxed on the withdrawal, it can be assumed that the repayment would create basis.

As an analogy, the Pension Protection Act of 2006 created another exception to the 10% early distribution penalty for "qualified reservist distributions" and allowed those distributions to be repaid. If the IRS treats birth or adoption withdrawals the same way, then the taxpayer would have to keep track of basis (on Form 8606 for IRA repayments and in the employee plan for company plan repayments) to ensure that the eventual distribution of the funds is tax-free.

Example: Aidan and his husband are the proud parents of a baby born in March of 2020. To help with the expenses, Aidan takes a $5,000 withdrawal from his 401(k) plan in April 2020.

Six months later, Aidan gets a hefty sales bonus. Aidan is still eligible to participate in the 401(k) plan and decides to immediately repay the withdrawal to an after-tax account in the plan. Even though the distribution was repaid in 2020, it is still taxable income to Aidan in 2020. The withdrawal is, however, exempt from the 10% early distribution penalty.

Without IRS guidance, it is not certain how Aidan's repayment will be treated. It is likely that it will be deemed to create basis and that those amounts will be tax-free when Aidan eventually takes a distribution of his entire 401(k).

SECURE Act Odds and Ends

The SECURE Act significantly impacted several other retirement areas. For example, while the age for RMDs was raised to 72, qualified charitable distributions (QCDs) are still permitted at age 70½. Even Congress admits this discrepancy will cause confusion.

Also, be aware that combining QCDs with newly allowed post-70½ deductible IRA contributions will subject the QCD to a peculiar mathematical formula that can make all or part of the QCD taxable. A post-70½ Roth IRA contribution will avoid such problems and may well be a better recommendation. Additionally, the new law allows taxable non-tuition fellowship and stipend payments to be treated as compensation for graduate or postdoctoral students, thus qualifying these payments for an IRA (or Roth IRA) contribution.

Another change affects foster care workers. These workers can exclude from taxable income certain "difficulty-of-care" payments from their employer. Under the SECURE Act, difficulty-of-care payments are now considered compensation for IRA and company plan purposes. Foster care workers can now make nondeductible IRA contributions and after-tax contributions to company savings plans. (The new difficulty-of-care payment rule applies to 2020 IRA contributions. For plan contributions, it applies retroactively to plan years starting after December 31, 2015.)

Furthermore, the SECURE Act provides new liability protection for plan sponsors who wish to offer annuities in a company savings plan. It will now be easier for the plan sponsor to satisfy its due diligence as a fiduciary when selecting an annuity provider. In addition, the sponsor is not compelled to select the lowest cost contract.

The new provisions practically mean that participants must direct any problems with plan annuities to the insurance company — *not to their employer.* Based on these changes, it is anticipated that more annuity products will become available as investment options within employer plans.

Planning Opportunities

While the SECURE Act presents a number of challenges and obstacles, it also creates a critical reason to meet with clients. Opportunities abound!

Trusts need to be reviewed and

potentially replaced. Beneficiary forms must be reevaluated. QCDs and Roth conversions remain valuable instruments. Life insurance leaps to the top of the list as an essential estate and tax planning vehicle. Client education is paramount.

If the SECURE Act has done anything, it has reinforced the necessity for current, thoughtful, forward-looking guidance. Trust rules have always been complicated and are even more so now. The stretch rules for the newly created "eligible designated beneficiaries" are complex.

Ch-ch-ch-ch-changes abound, and some are admittedly bizarre. Nevertheless, the SECURE Act is here, and the new rules contained within extend far and wide. Clients, financial planners, insurance agents, accountants, attorneys and the like — *all of us* — must turn and face the strange! ■

The SECURE Act's Unanswerable Questions

Guest IRA Expert

Natalie Choate, J.D.

Nutter McClennen & Fish LLP

Boston, MA

Saying that the Setting Every Community Up for Retirement Enhancement (SECURE) Act ends the stretch IRA opportunity for many people is accurate, but this aspect of the new legislation is far more nuanced. When the statutory rubber hits the estate plan drafting road, some of the rules are unclear. Indeed, until further guidance, regulations, or technical corrections are published, the answers to many SECURE Act questions are literally unknowable.

The SECURE Act's Stratification

The SECURE Act addresses estate planning for IRA owners and qualified plan participants by putting beneficiaries into three categories:

1. Eligible designated beneficiaries (EDBs)
2. Non-designated beneficiaries (NonDBs)
3. Designated beneficiaries (DBs)

For EDBs, the pre-SECURE Act rules largely remain in place, so life-expectancy-based schedules of required minimum distributions (RMDs) remain possible, permitting extended tax deferral. EDBs include surviving spouses, disabled and chronically ill (DCI) individuals, minor children of the participant, and beneficiaries less than 10 years younger than the account owner or plan participant.

The terms "disabled" and "chronically ill" are defined by reference to other sections of the tax code; minor children lose EDB status upon attaining majority (again defined by reference to other tax rules).

In another new twist, at the death of the EDB (or a minor's attaining majority), the life expectancy payout ceases to apply and a 10-year rule, explained below, kicks in.

> In another new twist, at the death of the EDB (or a minor's attaining majority), the life expectancy payout ceases to apply and a 10-year rule kicks in.

NonDBs include charities, the plan participant's estate, and trusts that are not see-through trusts. (See-through trusts are structured so they receive "designated beneficiary" treatment.)

For NonDBs, the old rules remain in place. Depending on whether the plan participant died before or after the required beginning date for RMDs, the account has to be emptied within five years or over the participant's remaining life expectancy at death.

All other beneficiaries are DBs, subject to the new 10-year rule. No annual RMDs are required but the inherited account must be distributed by December 31 of the year that contains the 10th anniversary of the date of the participant's death.

With this breakdown, the SECURE Act seems to provide straightforward distribution rules for inherited retirement accounts. Nevertheless, some troubling uncertainties persist.

Pre-2020 Deaths

The rules described are effective for deaths in 2020 and later years. However, many advisors have clients who inherited IRAs or qualified plans in prior years.

How are they affected by the SECURE Act? Generally, the 10-year rule becomes effective upon the death of the DB.

Example: Ben died in 2010 and left his IRA to his son Carl, who has been taking life-expectancy-based RMDs. Carl can continue to do so.

What if Carl dies in 2020 and his daughter Diane is the successor DB? Then, Diane will be subject to the SECURE Act's 10-year rule and will have to withdraw the entire remaining balance of this inherited IRA by December 31, 2030.

Continuing this example, an unknowable question arises because the SECURE Act ignores the possibility of multiple DBs. Suppose Ben, our pre-2020

decedent, had left his IRA to a see-through accumulation trust, which included life and remainder beneficiaries. (An accumulation trust permits some money to remain in the trust, whereas a conduit trust requires all plan distributions received by the trust to be distributed to the trust beneficiaries.).

Excluding beneficiaries who were merely potential successors of other beneficiaries, upon which trust beneficiary's death will the 10-year rule commence? The first to die? The oldest trust beneficiary?

One supportable position is that the 10-year rule won't become effective until after the deaths of all the designated beneficiaries who were living at the time of Ben's (the grantor's) death. For certainty, though, advisors must wait for IRS regulations or a court case to provide a resolution.

Matters of Trust

As the preceding paragraphs indicate, some of the SECURE Act's unanswerable questions relate to the use of trusts as an IRA beneficiary. One major blind spot of the SECURE Act is its apparent ignoring of the possibility that IRA trusts might have multiple designated beneficiaries.

This uncertainly applies when there are multiple EDBs of a conduit trust. Applying longstanding existing regulations to SECURE's new rules, we know that if the participant's minor child or a conduit trust for such child is named as retirement plan beneficiary the life expectancy payout will apply until the child reaches majority.

That said, what if the participant named a conduit trust for the benefit of multiple minor children? Does the 10-year clock start ticking after they all reach majority? Or when the oldest one reaches majority?

Similar uncertainty applies when there are multiple EDBs of an accumulation trust.

Example: Ellen names as IRA beneficiary an accumulation trust that provides life income to her sister Gina, an EDB who is less than 10 years younger than Ellen. Upon Gina's death, the remaining trust assets will go outright to her brother George, who is also less than 10 years younger than Ellen. In this scenario, all countable beneficiaries of the IRA trust are EDBs, but no EDB is considered the "sole" DB.

Would this trust qualify for life expectancy based RMDs? Based on whose life expectancy? Whose life expectancy would apply if the trust beneficiaries include an EDB who is disabled or chronically ill?

One major blind spot of the SECURE Act is its apparent ignoring of the possibility that IRA trusts might have multiple designated beneficiaries.

Serving Special Needs

Pre-SECURE law required that either an individual or a conduit trust for that individual's sole benefit must be named as plan beneficiary in order to be considered the sole designated beneficiary. SECURE doesn't change that rule — *except in the case of an accumulation trust for a disabled or chronically ill EDB, where SECURE eases the rule.*

Under a special rule for "applicable multi-beneficiary trusts," the SECURE Act provides that, in the case of an accumulation trust for the sole life benefit of a DCI, the life expectancy payout method shall apply to the distribution of the employee's interest; any beneficiary who is not a DCI shall be treated as a beneficiary of the DCI upon the DCI's death.

Thus, no beneficiary other than the DCI can receive distributions during the DCI's lifetime, but the DCI is not required to receive a pass-through of all plan distributions received by the trust during his or her life, which would be true for a conduit trust.

Drilling down into the SECURE Act's language could indicate that, with a see-through accumulation trust of which the sole life beneficiary is a DCI, the remainder beneficiaries' life expectancies are irrelevant for purposes of determining the applicable distribution period (ADP).

Another reading might suggest that the SECURE Act says that this type of accumulation trust can use the life expectancy payout based on the life expectancy of the oldest countable beneficiary, including remaindermen, as usual.

In sum, this rule says that such an accumulation trust (unlike all other accumulation trusts) can use the life expectancy payout method for RMDs. The unanswered question, though, is:

Whose life expectancy should be used? That of the DCI? Of the oldest trust beneficiary, as current regulations provide?

It appears the lawmakers intended the life expectancy of the DCI to apply, but it's not clear they actually said so in the SECURE Act. Therefore, until there is further guidance, it is advisable not to name a significantly older person as a remainder beneficiary of this type of trust. In addition, powers of appointment might be limited to younger individuals.

Sole Searching

Similar lack of clarity applies to a see-through accumulation trust for the sole life benefit of a single DCI, with the remainder

ED SLOTT'S
IRA ADVISOR

Editor-in-Chief
Ed Slott, CPA
Contributing Writers
Sarah Brenner, JD
Andy Ives, CFP®, AIF®
Ian Berger, JD
Copy Editor
Ryan Fortese
Graphic Design
Debbie Slott, D. Slott Design

Disclaimer and Warning to Readers: *Ed Slott's IRA Advisor* has been carefully researched to provide accurate and current data to financial advisors, taxpayers, and others who seek and use the information contained in this newsletter. Readers are cautioned, however, that this newsletter is not intended to provide tax, legal, accounting, financial, or professional advice. If such services are required, then readers are advised to seek the aid of competent professional advisors. This newsletter contains timely information about complicated tax topics that may eventually be changed, outdated, or rendered incorrect by new legislation or official rulings. The editors, writers, and publisher shall not have liability or responsibility to any person or entity with respect to any loss or damage caused or alleged to be caused, directly or indirectly, by the information contained in this newsletter.

ED SLOTT'S IRA ADVISOR

is a monthly publication made available for $125 annually by:

Smart Subscriptions, LLC
100 Merrick Road, Suite 200E
Rockville Centre, NY 11570
P: (877) 337-5688
E: newsletter@irahelp.com

ORDER ONLINE AT
IRAHELP.COM/ NEWSLETTER

©2020 All rights reserved
ISSN 1531-653X

Smart Subscriptions, LLC
100 Merrick Road, Suite 200E
Rockville Centre, NY 11570
No part of this publication may be reproduced, stored in a retrieval system, or transmitted in any form by any means without the prior written permission of Ed Slott, CPA and/or Smart Subscriptions, LLC.

going to another DCI and others. Regarding the type of trust that qualifies for this special break, the SECURE Act says that *"no individual (other than a [DCI]...) has any right to the employee's interest in the plan until the death of all such eligible designated beneficiaries with respect to the trust..."*

Example: Suppose a see-through accumulation trust has been set up for the sole lifetime benefit of James, who is disabled. The remainder beneficiaries are Kate, Jack, and Maggie, who will receive all of the trust's assets upon James' death.

Also suppose that Kate in this example is disabled, under the statutory definition. This trust would appear to flunk the test because Jack and Maggie could receive benefits prior to the death of Kate.

In short, the application of the SECURE Act to trusts with multiple DCIs remains unclear.

Subject to Change?

Another question likely to be asked by many is *whether the "longer of" rule still applies when a participant dies after her required beginning date (RBD) for minimum distributions.*

Under pre-SECURE law, the applicable distribution period for a DB, if the participant died after her RBD, was the life expectancy of the DB or the remaining life expectancy of the participant, if longer. That rule presumably still applies where benefits are left to an EDB: the payout period is the life expectancy of the EDB or of the participant, whichever is longer.

However, it's not clear whether the participant's life expectancy applies to a DB if such life expectancy is longer than the 10-year payout period created by the SECURE Act.

Advisor Action Plan

- Describe the impact of the SECURE Act to clients with large IRAs.
- Explain that money left to competent, nondisabled adult descendants would have to be distributed within 10 years after the year of death, potentially in high tax brackets then.
- Point out that naming a trust as IRA beneficiary because of specific concerns could lead to exceptionally high taxes due to the lofty tax rates on trust income.
- Explore other estate planning ideas to affected clients, such as buying life insurance, Roth conversions, leaving retirement benefits to a charitable remainder trust, and leaving such assets to a trust with a disabled or chronically ill, younger beneficiary. ■

Natalie Choate is of counsel with the Boston law firm of Nutter McClennen & Fish. Her practice is limited to consultations on estate planning for retirement benefits. Her book *Life and Death Planning for Retirement Benefits* is a leading resource for estate planning and money management professionals.

Miss Choate is a fellow and former Regent of the American College of Trust and Estate Counsel and former chairman of its Employee Benefits Committee. She serves as an editorial advisor for Trusts and Estates. Named "Estate Planner of the Year" by the Boston Estate Planning Council, she is listed in The Best Lawyers in America. The National Association of Estate Planners and Councils has awarded her the Distinguished Accredited Estate Planner designation. Her articles on estate planning topics have been published in *ACTEC Notes, Estate Planning, Trusts and Estates, Tax Practitioners Journal and Tax Management.* Miss Choate has lectured in 50 states, Canada, Puerto Rico, and the District of Columbia, and has spoken at the Heckerling, Notre Dame, and Southern Federal Tax Institutes, among others. Her comments on estate and retirement planning have been quoted in *The Wall Street Journal, Money, The New York Times, Newsweek, Forbes, Financial Planning and Financial World.* A Boston native, Miss Choate is a graduate of Radcliffe College and Harvard Law School.

You may contact her at (617) 439-2995 or nataliechoate@cs.com.

© 2020 Smart Subscriptions, LLC

SECURE Act

Retirement Plan Payouts to Beneficiaries Under the SECURE Act

(for deaths *after* 2019*)

***Extended Effective Dates**
The effective date for the elimination of the stretch and the new 10-year rule is generally for deaths after December 31, 2019. But that effective date is extended for two years (for deaths after December 31, 2021) for governmental plans, including 403(b) and 457(b) plans, and the Thrift Savings Plan. It is also extended for as long as two years for collectively-bargained plans, depending on the expiration date of the union contract.

Retirement Accounts Affected
The elimination of the stretch IRA and the new 10-year rule provisions apply to defined contributions plans, including 401(k), 403(b) and 457(b) plans, and traditional and Roth IRAs. They do not apply to defined benefit plans.

Under the SECURE Act, there are now 3 kinds of retirement plan beneficiaries for determining post-death payouts after 2019

1. Non-Designated Beneficiary (NDB)

2. Non-Eligible Designated Beneficiary (NEDB)

3. Eligible Designated Beneficiary (EDB)

1. Non-Designated Beneficiary (NDB)

No change from prior law

These are not people. Examples: Estate, charity or non-qualifying trust (non-look-through trust)

Post-death Payout Rules for NDBs
Nothing changes --- Based on whether the IRA owner or plan participant dies before or after the owner's required beginning date (RBD). The RBD is generally April 1 after the year of the 72nd birthday.

If owner dies before the RBD, the account must be withdrawn by the end of the 5th year after death – the 5-year rule.

If owner dies on or after the RBD, RMDs must be taken over the deceased IRA owner's (or plan participant's) remaining single life expectancy. This can now produce a post-death payout exceeding 10 years, until the remaining life expectancy drops below 10 years. However, RMDs must be taken in each of those years.

2. Non-Eligible Designated Beneficiary (NEDB)

New 10-year rule

All designated beneficiaries who do not qualify as EDBs (see #3 below).
Examples: grandchildren, older children, some look-through trusts

Post-death Payout Rules for NEDBs
No stretch IRA for deaths after 2019

No annual RMDs required

Entire account must be emptied by the end of the 10th year after death – the 10-year rule

3. Eligible Designated Beneficiary (EDB)

Stretch still applies

EDBs are a new category of beneficiaries created under the SECURE Act.

The SECURE Act exempts these beneficiaries from the 10-year rule.

EDBs must be designated beneficiaries.

5 Classes of Eligible Designated Beneficiaries
1. Surviving spouses
2. Minor children, up to majority – but *not* grandchildren
3. Disabled individuals – under the strict IRS rules
4. Chronically ill individuals
5. Individuals not more than 10 years younger than the IRA owner

Plus - Any designated beneficiary (including qualifying trusts) who inherited ***before*** 2020. These beneficiaries are grandfathered under the pre-2020 stretch IRA rules. In addition, trusts for the sole benefit of these EDBs should qualify as an EDB.

EDB status is determined at date of owner's (or plan participant's) death and cannot be changed.

Post-death Payout Rules for EDBs
These beneficiaries are unaffected by the new rules. But once they no longer qualify as EDBs, or die, the 10-year rule is applied for them, or for their beneficiaries.

Copyright © 2020 by Ed Slott and Company, LLC