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The SECURE Act's Impact on Retirement Planning and Estate Planning

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On December 20, 2019, President Trump signed a two-part spending bill funding the federal government through fiscal year 2020. Among the many provisions included in the spending bill is the Setting Every Community Up for Retirement Enhancement (SECURE) Act.

The SECURE Act enacts major changes to rules related to individual and employer-sponsored retirement accounts and may also materially alter estate plans incorporating retirement accounts. Three of the most significant changes are as follows:

(i) Required minimum distributions (RMD) begin at age 72 (rather than 70½) if you have not turned age 70½ by December 31, 2019;

(ii) Repeal of maximum age for traditional IRA contributions for those individuals who continue to work past 70½; and

(iii) Elimination of "stretch" RMD (required minimum distribution) provisions for non-spousal beneficiaries.

Let's focus on the latter item.

Under the prior law, RMD calculations for certain designated beneficiaries of inherited IRAs and other eligible retirement plans used the account beneficiary's life expectancy. Thus, if the beneficiary was considerably younger than the deceased owner, required withdrawals could be "stretched" for many years due to longer life expectancy. Under the SECURE Act, generally effective with respect to employees and IRA owners who die after December 31, 2019, the SECURE Act eliminates the stretch RMD option and requires certain beneficiaries to withdraw all assets within 10 years of inheriting the account. Significantly, this change does not apply to all beneficiaries, including surviving spouses, minor children, disabled individuals, the chronically ill, and beneficiaries not more than 10 years younger than the employee or IRA owner. With the exception of those five classes of beneficiaries, most beneficiaries will pay income tax on an accelerated basis and at higher rates!

Elimination of the stretch provisions may materially impact estate planning incorporating "pass through" trusts for children and younger generations that were designed to restrict access to the funds and limit the tax impact of RMDs. Bottom line, if your estate plan incorporated trusts to receive IRAs and other retirement plans for your descendants, as opposed to leaving same outright to them, then we need to redesign those trust provisions to bring them into compliance with the SECURE Act.

Naming a Spouse as a Beneficiary

Under the SECURE Act, a spouse named as an outright beneficiary still may (1) stretch the required distributions over the spouse's lifetime; and (2) roll over inherited benefits into the spouse's own IRA. Similarly, where a trust benefitting a spouse is named as beneficiary of a retirement plan (i.e., the Marital Trust), so long as the trust terms mandate that all RMDs of a plan to be distributed to the spouse, then the required distributions may be stretched over the spouse's lifetime. But, if the trust stipulates that the spouse is only entitled to receive annual distributions of income (and not the greater of the income or the RMD), then the retirement account will be subject to the 10-year payout rule, thereby accelerating the income tax payments on the RMD. Therefore, the terms of the surviving spouse's Marital Trust need to be reviewed to ensure a spouse's continued eligibility to stretch the IRA.

Naming Children as Beneficiaries

With some limited exceptions referenced previously, the majority of designations naming children as beneficiaries will now result in the accelerated 10-year payout of benefits. Adult children and trusts for adult children will now be subject to the new 10-year payout rule. Where minor children or trusts for minor children of the plan participant are named as beneficiaries, the 10-year payout clock will begin to run when the minor child reaches the age of majority. Other minors, such as grandchildren, are not considered eligible designated beneficiaries and are immediately subject to the 10-year payout rule.

Naming a Trust as a Beneficiary

Prior to the enactment of the SECURE Act, "conduit trusts" were often used in conjunction with the lifetime stretch rules for distributing retirement accounts to beneficiaries. A conduit trust is one in which all required distributions from a retirement account received by a trust are distributed at least annually to the trust beneficiary, with income associated with the required distributions then being taxed to the beneficiary at his or her individual income tax rate. Using this trust structure has historically minimized the income tax impact on required distributions. But, with the

new 10-year payout under the SECURE Act, conduit trusts could cause punitive income tax consequences. Beneficiaries will now have to realize a significant amount of income over a shorter period of time since all plan benefits must be distributed outright to beneficiaries within the 10-year term, likely resulting in higher income tax rates. In other words, conduit trusts will cause large lump-sum distributions to the beneficiary after 10 years if distributions are not made 1/10th per year over 10 years. Further, trust with conduit provisions will no longer provide the long-term control or protection of retirement benefits and their proceeds for beneficiaries that many plan participants previously expected.

Planning Recommendations

Plan participants may consider naming an "accumulation trust" as the beneficiary of a retirement account instead of a conduit trust if they wish to avoid the retirement account being distributed in full to the beneficiary within the 10-year term. An accumulation trust allows the required distributions to collect inside a trust with the Trustee maintaining discretion regarding distributions to trust beneficiaries. However, the retirement account would be required to distribute to the trust in full under the new 10-year payout rule, resulting in accelerated income tax payments at higher tax rates charged to the trust (though actual distribution to a beneficiary will still be taxed at the beneficiary's rate). Even if you utilize an accumulation trust, you still have to figure out how to pay the tax bill since there are very few options to avoid the tax bill. Bottom line, terms of trusts in existing estate plans should be carefully reviewed in conjunction with the new SECURE Act terms to ensure that a plan participant's intentions are still met.

Impact on Roth IRAs

Roth IRAs are also subject to the accelerated 10-year payout rule under the SECURE Act. However, since distributions from Roth IRAs are not subject to income tax, the accelerated income tax liability is not a concern.

Planning Recommendations

Where IRA owners have a lower income tax bracket than the intended beneficiary of an IRA (which is likely the case if the beneficiary is a trust due to the compressed tax brackets for trusts), IRA owners may want to consider a Roth conversion during life. As such, the IRA owner would pay income tax at his or her income tax rate, with distributions passing income-tax-free to the named beneficiary. We anticipate increased interest in Roth conversions post SECURE Act!

What to Do Now

The SECURE Act is the first significant change to retirement planning legislation in nearly two decades and will impact ever individual owner and beneficiary of a retirement account. All retirement plan participants should review their current retirement plan beneficiary designations in conjunction with the review of their estate planning documents. If you would like to discuss how these new laws may impact your retirement or estate planning, please contact a member of the Trusts and Estates Department.

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Sol is a Director in the Dallas office, with over 39 years' experience in probate administration, trusts and estate planning law, as well as, asset protection. He is involved in structuring family estates to maximize the amount of assets that pass to succeeding generations through the use of various types of trusts and business entities that will minimize the amount of shrinkage due to "transfer taxes" pertaining to such transfers (i.e, the estate, gift and generation skipping taxes). His practice includes legal consultation and structuring of business and family investment entities to protect key family assets from litigation risks. He counsels clients that estate planning done correctly is multi-generational. His philosophy is that estate planning is a lifetime "process" of planning for the accumulation, conservation and distribution of wealth between the generations.

Sol has received the designation as an Accredited Estate Planner from the National Association of Estate Planners, 1995, and was selected to "5-Star" Wealth Manager in 2010-2019 and to the Texas Super Lawyers list in 2011-2019.

Admitted

- Texas, 1980
- U.S. Tax Court

Education

- LL.M. Estate Planning, 1982, University of Miami in Miami, Florida
- J.D., 1980, Southwestern University
- B.A., cum laude, 1974, The University of Texas

Affiliations

- Dallas Bar Association
- American Bar Association
- Dallas Estate Planning Council
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Honors and Awards

- Accredited Estate Planner
- Named to the Texas Super Lawyer list in the area of Trusts and Estates, 2011-2019
- Selected as a "5 Star" Wealth Manager, 2010-2019

Publications and Presentations

- "Are Living Trusts for You," T.A.L.S. Docket (March 1991)
- "Structural Considerations for a FSC," Prentice-Hall, U.S. Taxation of International Operations (October 9, 1985)
- "Choosing a FSC Jurisdiction," Prentice-Hall, U.S. Taxation of International Operations (September 25, 1985)
- "The Foreign Sales Corporation-An Analysis of Its Impact, Attributes and Planning Opportunities after the 1984 Tax Reform Act," Prentice-Hall, Tax Ideas (Fall 1985)
- "Section 401(k) Plans-An Alternative to an IRA," Warren, Gorham & Lamont, The Review of Taxation of Individuals (Spring 1985)
- "Auld Lang Syne for Professional Personal Service Corporations," State Bar of Texas, Texas Bar Journal (May 1983)

Activities

- Estate Planning Instructor, SMU Certificate Program for Financial Planning (2010-present)
- Adjunct Professor in Estate Planning, School of Business, University of Texas-Dallas (2015-2017)
- Estate Planning Instructor, Graduate School of Business at the University of Dallas (1995-2010)
- Professional Development Institute at the University of North Texas (May 1993-June 2010)
- Southeastern Paralegal Institute (June 1992 – May 1998)
- Judicial Law Clerk for Judge Jack Swink in the Probate Court of Los Angeles (1979)