The SECURE Act

Last Minute Legislation Includes Pension and IRA Changes

With Social Security funding facing issues and Pensions disappearing at rapid rates, Congress took some small steps under the Secure Act with some retirement enhancements. The Secure Act was passed by the House in May 2019 with a 417-3 vote. There are some important changes to Individual Retirement Accounts, 401k's, and Pensions. We desire to highlight some of these, but this is only some of the many SECURE ACT provisions included in the Appropriations Act.

IRA Changes

It's becoming harder and harder to retire, and the worry about running out of money and being left with just Social Security is a common concern. Also, Social Security's inverse pyramid funding issues are still not yet settled. Thus, you never know if there will be a cut coming to Social Security benefits.

The SECURE ACT pushed back the Required Minimum Distributions (RMDs) from your traditional IRA from age 70 ½ to age 72. The age change applies to distributions required to be made after Dec. 31, 2019, with respect to Individuals who attain age 70½ before and after that date.

- If you turned 70 ½ in 2019, then unfortunately, your first RMD must be taken by April 1, 2020.
- If you turn 70 ½ as of 01/01/2020, you do not have to take your RMD until you turn 72 years old.

IRA contributions after age 70 ½

They only pushed the RMD back. Yet beginning in 2020, the age limit to contribute to your IRA has been completely eliminated. Before, contributions to your IRA were not allowed after the year the Taxpayer turned 70 ½. Now you can contribute to an IRA, if you have earned income after that age of 70 ½.

Qualified Charitable Distribution

Pushing the RMD age out to age 72 does not change the Qualified Charitable Distribution (QCD) rule.

A Taxpayer who is 70 ½ may make a QCD and reduce his or her Required Minimum Distribution. Because IRA contributions are now deductible for those who qualify for the Qualified Charitable Distribution (QCD) provision, the SECURE Act reduces the allowable QCD by the IRA deduction allowed for a Taxpayer over 70 ½.

Example: Randall made traditional IRA contributions at age 71 and 72 for a total of $14,000. A few years later, Randall directs the custodian of his IRA to make a Qualified Charitable Distribution of $25,000 to the Feed the Hungry. The first $14,000 of the distribution is not treated as a QCD. Thus, Randall will include the $14,000 of the distribution as taxable income and deducts $14,000 to the Charity on his Schedule A as a charitable contribution. The remaining $11,000 would be a Qualified Charitable Distribution.

Changes to Non-Spouse Beneficiaries

When you were the Beneficiary on someone's IRA who passed away, and that person was not your Spouse, you were allowed to do what is called a “stretch” distribution. The term stretch distribution meant you were allowed to take the distributions over your lifetime. The “stretch” distribution period for Non-Spouse inherited IRAs is now reduced to a 10-year maximum. Within the 10-year period, there are no required distributions. But the entire Inherited Retirement Account must be distributed by the end of the 10-year period. Make sure you’re planning with your Tax Professional to take the distributions in the most tax efficient way possible. A change from prior law, the 10-year period applies regardless of whether the Plan Participant or IRA Owner dies before or after reaching their required age for taking distributions. If you already receive stretch distributions from an inherited IRA you are grandfathered in and the new law will not affect you. These changes will apply to distributions for a Non-Spouse Beneficiary if the Plan Participant or IRA owner’s death occurs after Dec. 31, 2019, thus as of Jan. 1, 2020.

Example: Joe’s father passes in 2020 and had named Joe as the Beneficiary of his $500,000 IRA.
Joe may withdraw funds from the IRA as he wishes, but the entire account balance must be withdrawn by the end of the 10-year period.

The 10-year distribution limit does not apply to “Eligible Designated Beneficiaries”.
These include:

- a Surviving Spouse[2];
- a Minor Child[3] (the exception for a minor Child no longer applies once the Child reaches the age of majority and the remainder of the distributions to that Individual must be completed within 10 years after that date);
- a disabled Individual (§72(m)(7));
- a chronically ill Individual (§7702B(c)(2)); and
- an Individual who is not more than 10 years younger than the deceased participant or IRA Owner.

Distributions for Birth and Adoption

The new law allows for up to a $5,000 Distribution from an IRA and a Qualified Pension Plan for the birth or adoption of a Child, and is per Individual. The withdrawal will be excluded from the 10% early withdrawal penalty. To meet the requirements of the qualified birth or adoption distribution, the Individual must take a distribution during a one-year period beginning on either the date of birth of the Child, or the date of the final adoption of the Child (under age 18). An Individual taking a distribution for the birth or adoption of a Child may make an additional contribution back to the plan from which the distribution was made or to an IRA. The IRS will need to provide timing rules for the repayment.

Tax Planning

Each Spouse may take a $5,000 distribution, if each Spouse has a Retirement Plan Account.

The distribution will not be treated as a qualified birth or adoption distribution unless the Taxpayer includes the name, age, and Taxpayer identification number of the Child or eligible Adoptee on the Taxpayer’s tax return for the taxable year. This change is effective for distributions made after Dec. 31, 2019, as of Jan. 1, 2020.

Two amounts treated as compensation for IRAs

Certain taxable non-tuition fellowship and stipend payments to graduate and post-doctoral students are treated as compensation for IRA purposes. This change is effective for taxable years as of Jan. 1, 2020.

Excluded difficulty of care payments (§131) are treated as compensation for determining non-deductible IRA contributions. This change is effective for contributions made after Dec. 20, 2019.

401(k) Changes

Part-time Employees

401(k) plans are required to offer participation to full-time, long-term and part-time Employees. Employers with 401(k) plans must offer Employees who work between 500 and 1,000-hours a year an additional means to participate in the plan. The rule change only affects 401(k) cash or deferral arrangements, and no other Qualified Plans. A part-time Employee is eligible to participate in the employer's 401(k) plan, if the Employee has at least 500 hours of service in three consecutive 12-month periods.

The change applies to plan years beginning after Dec. 31, 2020 and this year does not count as year of service, so the earliest that a part-time Employee will be able to participate in the 401(k) plan is 2024.

Automatic enrollment credit for Small Employers

To encourage participation, a new tax credit of $500 for a three-year credit period is allowed for small employers adding an auto-enrollment provision to their plans. The credit applies for taxable years beginning after Dec. 31, 2019, for Tax Year 2020.

Automatic enrollment percentage increased

Beginning in 2020, the SECURE Act allows the plan to set the automatic enrollment percentage to as high as 15% (previously has been at 10%).

Annuity offerings in 401(k) plans

The SECURE Act updates the safe harbor provision for Plan Sponsors to offer Annuities in their 401(k) plans to ease liability concerns. New ERISA §404(e) provides a Fiduciary Safe Harbor for Fiduciaries selecting a "Lifetime Income Provider." When selecting an Annuity Provider, the Fiduciary must engage in "an objective, thorough and analytical search" of Providers and obtain several written representations from the Annuity Provider selected.

The SECURE Act also provides that pension plans may make a direct Trustee-to-Trustee transfer to another Employer Plan or IRA of lifetime income investments in the form of a Qualified Plan Distribution Annuity, if a lifetime income investment is no longer allowed as an investment option in a plan.

Retirement Plans for Small Employers

Several changes are made to encourage Small Employers to offer retirement benefits to their Employees, such as:

Pension plan start-up cost credit

The credit for a Small Employer starting a pension plan, such as a 401(k), 403(b), SEP IRA or SIMPLE IRA, has been increased for taxable years beginning after Dec. 31, 2019. For the first credit year and each of the two taxable years immediately following the first credit year, the credit is the greater of—

(A) $500, or
(B) the lesser of—

(i) $250 for each Employee of the eligible employer who is not a highly compensated Employee and who is eligible to participate in the eligible employer plan maintained by the eligible employer, or (ii) $5,000.

> **Example:** Ashley starts a SEP IRA in 2020 for her and one Employee. She is entitled to a start-up credit of $500 (2 x $250) for 2020, 2021 and 2022.
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> **Example:** David starts a 401(k) plan for him and his 20 Employees. Ron is entitled to a startup credit of $5,000 (21 x $250 limited to $5,000) for 2020, 2021 and 2022.

Multiple Employer plans

Small Employers of two (2) or more Employees may come together to participate in a new class of pooled Multiple Employer Plans (MEPs). A MEP essentially allows Small Employers to join together to offer pension plans with (presumably) lower administrative costs. A critical factor that made Employers skeptical of the MEP was the IRS's "bad apple" rule. The IRS said that if one (1) Employer in the plan defaulted, the whole plan was disqualified. The SECURE Act now provides that if a single Employer defaults, the remaining plan maintains its qualified status. The SECURE Act requires the MEP to be administered by a "Pooled Plan Provider." Generally, changes apply to plan years beginning after December 31, 2020.

Miscellaneous Changes

Establishing a Retirement Plan

Beginning in 2020, Employers may adopt Retirement Plans that are entirely Employer funded up to the due date of the tax return, including extensions. Current law requires the Employer to establish their plan by December 31st (or the last day of their fiscal year).

Kiddie Tax

For tax years beginning after Dec. 31, 2019, the unearned income of certain Children is again taxed at the Parents' tax rate. In 2018 and 2019, the Tax Cuts and Jobs Act taxed the unearned income of Children using the much higher trust tax rates. BUT NOW, SECURE Act allows a Taxpayer to elect (at such time and in such manner as the IRS may provide) for the change to apply to taxable years beginning in 2018, 2019, or both (as specified by the Taxpayer in his or her election).

529 Plan

1. ***Student loans***

   The SECURE Act provides that up to $10,000 (reduced by the amount of distributions so treated for all prior taxable years) may be withdrawn from a 529 Plan for the purpose of paying principal or interest on any Qualified Education Loan of the Beneficiary or his or her Siblings. This is effective for distributions made after Dec. 31, 2018.

   Note: *The paid off loan interest with the distribution is not deductible.*

2. ***Apprenticeship Programs***

   The SECURE Act also provides that a Qualified Distribution includes: tuition, books, supplies and equipment required for Apprenticeship Programs, if the program is properly registered and certified by the Department of Labor. Effective for distributions made after Dec. 31, 2018.

Pension Provisions in Disaster Tax Relief

New rules apply to Individuals who had a principal residence in a Federally declared disaster area and who suffered an economic loss as a result of the disaster. The disaster must have occurred from Jan. 1, 2018 through Feb. 18, 2020 (60 days after the enactment of the law).

1. ***Qualified Disaster Distributions***

   The Appropriations Act also includes provisions relating to qualified disaster[5] distributions from Retirement Accounts. A Qualified Disaster Distribution is one made beginning on the first day of the incident period of the qualified disaster and ending on the date which is 180 days after Dec. 20, 2019 (the date of the enactment).

   Qualified Disaster Distributions can be made up to $100,000, and:

   - Are exempt from the 10% early withdrawal penalty,
   - Are exempt from mandatory withholding requirements,
   - Are treated as evenly distributed over a three (3) year period, and
   - May be repaid within three (3) years of the distribution.

2. ***Pension Plan Loans for Qualified Disasters***

   The limit on loans from Retirement Plans for a qualified disaster increased to $100,000 (was $50,000). Disaster loan repayments are delayed for up to one (1) year.