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The Setting Every Community Up for Retirement Enhancement (SECURE) Act was added to a year-end spending bill and signed into law with bipartisan support on December 20, 2019. The bill passed the House of Representatives in May but was held up in the Senate, and it was unclear whether it would survive even a few days before it was passed. SECURE is the first significant retirement legislation in 13 years—it is designed to make it easier for Americans to save for retirement, although there are also some revenue-raising law changes that will negatively impact certain IRA holders.

The changes become official on January 1, 2020, and will affect your ability to save for retirement, access your money during retirement, and pass along your wealth to heirs. We highlight below the changes we feel are the most important for individual investors.

Required Minimum Distributions. The start date for Required Minimum Distributions (RMDs) changes from age 70.5 to 72. This change applies to everyone who did not take an RMD in 2019. In other words, if you are already taking RMDs or took your first distribution in 2019, you must continue without changes. Everyone else can wait until age 72 to take their first RMD.

The rules continue to allow you to defer your first distribution as late as April 1 of the year after you reach age 72, however you will have to take two distributions that year if you wait. Because of this, most clients take their first distribution before December 31.

This start date change to age 72 will not only reduce the total amount of required withdrawals over your lifetime, but pending IRS changes to their life expectancy tables, will likely also reduce the dollar amount of required withdrawals each year. Overall, this should allow the aggregate retirement savings of Americans to grow larger and be withdrawn more slowly, helping to offset the cumulative effects of longer lifespans and inflation. However, the changes will likely only have a minimal beneficial effect. The Employee Benefit Research Institute estimates that RMDs will only decrease by about 7-8% at most (assuming a 10% increase in life expectancy and a two-year increase in start date).

IRA contributions allowed past age 70.5. Those with earned income past age 70.5 can continue contributing to IRAs. The old rule prohibited IRA contributions past age 70.5 even if you continued to work. This restriction did not apply to 401(k) plan participants, so this change removes that inconsistency. There are no age-based restrictions on contributing to Roth IRAs and that will continue to be the case.

The time perod for "Stretch IRAs" is reduced. Non-spouse beneficiaries of an inherited IRA are no longer required to take RMDs based on their age, but must withdraw all funds by the end of the 10th year after the IRA owner passes away. This applies to IRAs, 401(k)s, and other defined contribution assets that are inherited in 2020 and beyond. The old rules required RMDs to be withdrawn each year, but the principal of the inherited IRA could be stretched over the lifetime of the inheritor. The rules for spousal rollovers remain unchanged—surviving spouses can continue to rollover IRAs as their own.

For younger beneficiaries, this could mean a significant loss of income and acceleration of taxes because under the old rules it was possible to continue an inherited IRA for many decades. There are some notable exceptions to the new rule however. Lifetime distributions are allowed if the beneficiary is a minor at the time of receiving the money, disabled, chronically ill or not more than 10 years younger than the deceased IRA owner.

529 plans made more flexible. Qualified education expenses are currently limited to $10,000 in K-12 tuition and certain college costs. Under the SECURE Act, qualified expenses are expanded to include student loan payments and the costs of apprenticeship programs. 529 plan account holders will be allowed to withdraw up to $10,000 for payments toward qualified student loans. And the dollar limit applies to the plan beneficiary and each of their siblings, thus allowing a family with three children to pay off up to $30,000 of aggregate student loans.

One strategy to take advantage of this change is to have a grandparent-owned 529 plan pay off student loans after graduation rather than paying college costs during school. This strategy works because distributions from a grandparent-owned 529 are normally reported as untaxed income on a student's financial aid application. This potentially reduces aid by up to 50% of the distribution amount. This 50% penalty can be avoided by waiting and paying off loans after graduation.

Barbara Roper, Director of Investor Protection
Consumer Federation of America

Expanded annuity information and options inside 401(k)s.
The insurance industry lobbied heavily for this aspect of the legislation, which make it easier for them to sell annuities inside 401(k) plans. First, the SECURE Act requires plan sponsors to provide annual "lifetime income disclosure statements" to participants. These statements will show how much you could get each month if you purchased an annuity with your 401(k) balance. Second, the new law makes it easier for sponsors to offer annuities and other "lifetime income" options by removing some of the legal risks associated with these products. Specifically, the responsibility of ensuring that products offered are appropriate for participants now falls on the insurance company rather than the employer.

Consumer advocates have expressed concern about this part of the legislation. For example, Barbara Roper, Director of Investor Protection at the nonprofit Consumer Federation of America, told the Wall Street Journal, "Given the prevalence of high-cost, low-quality annuities, we don't start with the thought that this is a great idea." We agree that this could be more of a negative than a positive. There are times when annuities can make sense in a retirement plan, but it may be difficult for most investors to properly evaluate these products and make a smart decision. The cost of making a mistake might be high—annuitization of one's retirement assets can result in large fees and penalties if done incorrectly.

Please let us know if you want to discuss how any of these changes affect your situation. We look forward to helping you understand the new law and implement new strategies that might be needed.

As always, thank you for you continued trust and confidence.

Warm regards,

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