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'Money $ense': What you need to know about the SECURE Act

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ON DEC. 20, 2019, President Trump signed a new piece of retirement legislation into law called the Setting Every Community Up for Retirement Enhancement (SECURE) Act. Among the provisions are those impacting required minimum distributions (RMDs), IRA contributions, and Section 529 Plans. Here is a brief summary of these provisions.

One of the most significant changes involves how non-spouse beneficiaries must withdraw money from inherited retirement accounts, such as IRAs and 401(k)s. Previously, a beneficiary inheriting a retirement account could take distributions over his or her life expectancy, which was the so-called ability to “stretch” out the distributions. Certain beneficiaries will now have a 10-year window from which to withdraw all of the funds from an inherited account. The effect of the change might be a larger distribution that pushes the beneficiary into a higher tax bracket.

There are some exceptions to this rule. Certain beneficiaries, such as surviving spouses, minor children, disabled individuals and beneficiaries who are less than 10 years younger than the original account owner, will be exempt from these new RMD rules. These types of beneficiaries might still be able to use their own life expectancy when calculating RMDs.

There is also a change to the RMD rules for retirees. Under the old rules, retirement account owners generally had to take funds from their accounts by April 1 of the year following the year they turn age 70½. The act will change the starting age to 72. Workers who are age 72 but still working may not have to take an RMD from the plan of the employer they work for. Under these circumstances, it is best to check with the plan administrator.

For those wanting to make a qualified charitable distribution (QCD) from an IRA, the rules under the SECURE Act still allow a start date of age 70½. A QCD is a contribution directly from a retirement account to a charity. There is no tax deduction for making the contribution, but no income is taxed on the distribution either.

The SECURE Act also made a change to IRA contributions. It used to be that once an individual reached age 70½, that person could no longer contribute to an IRA. As long as there is earned income to support the contribution and the individual meets the income thresholds, an IRA contribution can potentially be made.

For those considering adopting a child or who have a newborn on the way, there is now a penalty exception for taking money out of an employer plan to help pay the costs. Generally, taking amounts from a retirement plan when the participant is under age 59½ incurs not only tax, but also a 10% penalty. Now, up to $5,000 may be withdrawn for expenses directly related to the birth or adoption of a child. Note that the income tax still must be paid on the funds.

On the education front, the good news here is that the definition of qualified expenses has been expanded for Section 529 Plans. These plans are vehicles that can be used to accumulate funds to pay for college expenses. Earnings on contributions to the plan are tax free. If the money withdrawn from the plan is used to pay for qualified education expenses, the money retains its tax free nature. The act now considers certain apprenticeship programs and the repayment of student loans up to $10,000 to be qualified expenses. The $10,000 is a lifetime limit and applies per person.

These are just some of the provisions in the SECURE Act. As with any new legislation, there will be clarifications to the rules as time goes on. Most changes are effective as of Jan. 1. The Section 529 Plan provision is effective for distributions made in 2019. As the law is complex, we would suggest speaking with a certified financial planner or a personal tax adviser as to how the changes will impact your situation.

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