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A Publication of Bowditch & Dewey's Estate, Financial & Tax Planning Group

SECURE ACT: Foreseeable Change in 'Stretch IRA' Distribution Rules

BY KATHERINE R. DORVAL • DECEMBER 9, 2019

The Setting Every Community Up for Retirement Enhancement Act of 2019 (or the "SECURE ACT") passed the House of Representatives on May 23, 2019, by an overwhelming majority of 417-3. It's getting bipartisan support due to the wide range of critical reforms it would make to the retirement system. Included in the Act under the heading of "Revenue Provisions," however, is a significant change to the income tax deferral benefits currently available for inherited retirement accounts.

The Internal Revenue Code requires that minimum annual distributions from Qualified Retirement Plans and Individual Retirement Accounts be made following the death of the owner. The dizzying complexity of the minimum required distribution (or "MRD") rules has been the topic of lengthy books and seminars, and this is not intended to be a comprehensive account of the rules. In a nutshell, the current rules generally allow for the MRDs to be stretched over the length of the oldest individual beneficiary's life expectancy (and, as a result, defer the income taxation of the distributions).

The SECURE ACT, if passed, will limit the "stretch" deferral period such that distributions would need to be completed by the end of the 10th calendar year following the death of the owner. There are four exceptions under the Act, allowing for longer distribution periods for the following individuals:

- 1) surviving spouses,
- 2) disabled or chronically ill individuals,
- 3) individuals who are not more than 10 years younger than the IRA owner, and
- 4) minor children of the IRA owner.

The new rule, however, would have a wide application. Parents often name their adult children as the primary or

contingent beneficiaries of their IRAs. For younger beneficiaries, this could have a significant effect.

If a parent names a child as a beneficiary of an IRA and that child turns 40 the year after the parent dies, under the current rules, that child can stretch the MRDs over his or her life expectancy, which would be 43.6 years according to the IRS "Single Life Table." If the SECURE ACT is passed, the same beneficiary would have only 10 years (versus 43.6 years) to stretch out the distributions of the account balance. The intent is clearly to raise tax revenue resulting from the faster, greater MRDs. The effect, however, is to reduce the tax benefits of "Stretch IRAs."

The Act's progress is currently stalled in the Senate after a failed attempt in November for unanimous approval (thwarted only by three Senators). Though the SECURE ACT may take a lot more time to get proper approval, it's likely that change is in the air.