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PRODUCT & SERVICE GUIDE

New SECURE Act Expands Retirement Savings Opportunities

Tax practitioners can consider sharing this information with their clients and meeting with them to take advantage of the retirement planning opportunities – never a bad thing! Here is a summary of the higher-impact provisions of the SECURE Act.

Feb. 23, 2020

On Dec. 20, 2019, the Setting Every Community Up for Retirement Enhancement Act (SECURE) was signed into law. Overall, this new legislation loosens the rules

surrounding retirement plans, and expands the opportunities for taxpayers and families to save for retirement. Many of the measures go into effect beginning in tax year 2020.

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Required Minimum Distribution Age Raised From 70½ to 72

Prior to 2020, participants in employer-sponsored retirement plans (401(k) plans, for example), traditional IRAs and individual retirement annuities needed to begin taking required minimum distributions (RMDs) from their plans by April 1 of the year following the year they turned 70½ years old. Under the SECURE Act and for distributions required to be made after Dec. 31, 2019, the age at which individuals must start taking distributions from these retirement plans has increased from 70½ to 72.

- **Rationale:** The existing rule attempts to get taxpayers to spend their retirement savings during their lifetime instead of transferring wealth to beneficiaries through estate planning.

Modification of Required Minimum Distribution Rules After Death

In general, owners of tax-favored employer-sponsored retirement plans and IRAs must take distributions over their life or life expectancy (RMDs). If the plan participant or IRA owner dies before 2020, spousal and non-spousal beneficiaries are allowed to stretch out the required distributions over the beneficiary's life or life expectancy.

For deaths of plan participants or IRA owners beginning in 2020, distributions to most non-spouse beneficiaries need to be distributed within 10 years after the plan participant or IRA owner's death. Exceptions to the 10-year rule for distributions include the following:

- A surviving spouse of the plan participant or IRA owner.
- A child of the plan participant or IRA owner who hasn't reached majority.
- A chronically ill individual.
- Another person who isn't more than 10 years younger than the plan participant or IRA owner.

For individuals who fall under one of the exceptions, they will continue to take distributions over their life or life expectancy.

Repeal of Maximum Age for Traditional IRA Contributions

For contributions made for tax years beginning after 2019, the SECURE Act allows individuals of any age to make contributions to a traditional IRA, assuming there is enough compensation. Prior to this rule change, taxpayers were not allowed to make an IRA contribution once they reached age 70½ by the close of the year. The restriction doesn't apply to Roth IRA contributions.

- **Rationale:** Americans are living longer and many are continuing to work past 70½ years old.

For qualified charitable distributions (QCD) made after 2019, the taxpayer's QCD is reduced by the excess of: 1) the total amount of IRA deductions allowed after reaching age 70½, over 2) the aggregate amount of reductions in prior years.

Penalty-free Retirement Plan Withdrawals for Births and Adoptions

Beginning in 2020, taxpayers can take up to $5,000 (for each spouse) of penalty-free retirement plan distributions for expenses related to the birth or adoption of a child. In general, retirement plan distributions are included in income, and unless an exception applies, distributions before the recipient turns 59½ years old are subject to a 10 percent early withdrawal penalty.

Long-term/Part-time Workers Allowed to Participate in 401(k) Plans

Under current law, employers are allowed to exclude part-time employees who work less than 1,000 hours per year from participating in defined contribution plans. Under the new law, and for plan years beginning after Dec. 31, 2020, employers must allow employees working at least 500 hours per year for at least three consecutive years to make elective deferrals.

- **Rationale:** Women are more likely to work part-time and can be excluded from participating in retirement plans.

Taxable, Non-tuition Fellowship and Stipend Payments Treated as Compensation for IRAs

Beginning in 2020, graduate and post-doctoral students who receive taxable, non-tuition fellowship and stipend payments are allowed to treat the payments as compensation for IRA contribution purposes. IRA contributions cannot exceed a taxpayer's compensation included in gross income.

Increased Credit Limit for Small Employer Pension Plan Start-up Costs

Small business owners are allowed to take a tax credit for establishing a qualified retirement plan, such as a SIMPLE IRA or SEP plan. The credit is the lesser of $500 or 50 percent of the start-up costs.

For tax years beginning after Dec. 31, 2019, the SECURE Act increases the credit to the greater of $500 or the lesser of $250 multiplied by the number of non-highly compensated individuals eligible to participate or $5,000.

- **Rationale:** The increased credit makes it more affordable for small businesses to establish a retirement plan.

Small Employer Automatic Enrollment Credit

For tax years beginning after Dec. 31, 2019, the SECURE Act establishes a $500 tax credit for employers who set up a new 401(k) plan or SIMPLE IRA plan with an automatic enrollment feature. The credit helps offset plan start-up costs and is in addition to the already existing pension plan start-up credit. You also qualify for the credit if you convert an existing plan to one with automatic enrollment.

- **Rationale:** Retirement plans with automatic enrollment have proven to increase participation, leading to more retirement savings.

Expansion of Section 529 Plans (qualified tuition programs)

For distributions made after Dec. 31, 2018, qualified higher education expenses under Section 529, which allows for tax-free treatment, now include costs associated with registered apprenticeships. and up to $10,000 of qualified student loan repayments (principal and interest).

Kiddie Tax Changes

Prior to the Tax Cuts and Jobs Act (TCJA), the net unearned income of a child (under 19 years old or a full-time student under 24 years old) was taxed at the parent's tax rates, if the parent's rates were higher than the child's rates. For tax years beginning

after 2017, the TCJA changed the rule so that the unearned income of the child would be taxed at trust and estate tax rates.

The SECURE Act repeals the kiddie tax rules that were added by TCJA, effective for tax years beginning after Dec. 31, 2019. You may elect to apply the pre-TCJA rules in 2018 and 2019. By the way, a child's earned income is taxed at single rates and this has not changed.

- **Rationale:** The TCJA changes unfairly increased the tax on certain children.

Failure to File Penalty Increased

For tax returns with due dates after Dec. 31, 2019, the failure to file penalty is increased to the lesser of $435 or 100 percent of the tax due (from the lesser of $205 or 100 percent of the tax due). The penalty applies when a return is more than 60 days late and the taxpayer cannot show reasonable cause for the late filing. If the failure to file penalty and the failure to pay the tax penalty both apply in the same month, the failure to file penalty is reduced by the failure to pay penalty.

- **Rationale:** The penalty encourages timely and accurate returns being filed.

Educate Your Clients

Tax professionals can take advantage of this new legislation as another way to educate their clients and buttress their role as a trusted advisor through retirement planning.

Resource

Ways and Means Committee Summary

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