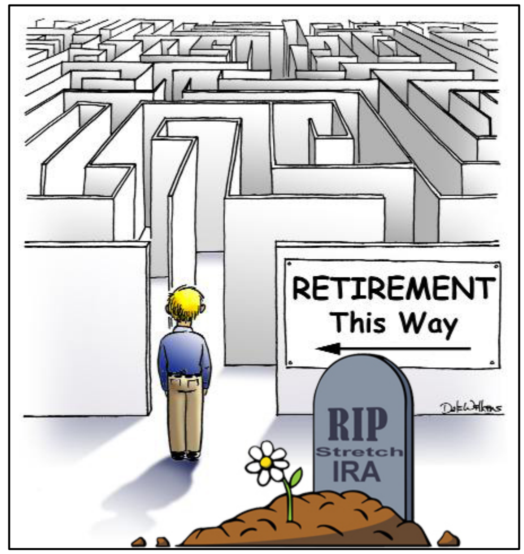
Reprinted from the
Lexington Minuteman

CWM
COROMANDEL WEALTH MANAGEMENT

July 2019

The Demise of the Stretch IRA

Navigating the Retirement Maze



"Retirement is like a long vacation in Las Vegas. The goal is to enjoy it the fullest, but not so fully that you run out of money."

– *Jonathan Clements, author, former Wall Street Journal columnist*

"Ladies and gentlemen the members of Congress present you with (drum roll, along with appropriate pause)… the SECURE Act of 2019."

Well not just yet, as the different versions of the bill need to be reconciled by both chambers – the Senate has its own version, the Retirement Enhancement Securities Act (RESA) – and signed by the President. Considering that it passed the House a vote of 417 to 3, a bipartisan margin greater than if there had been a vote on whether the earth is round, it will most likely be enacted before year-end.

The "Setting Every Community Up for Retirement Enhancement" (SECURE) Act is the largest overhaul in retirement legislation since 2006. It includes provisions that will enhance the ability of workers to prepare for retirement, along with one that isn't quite as positive. I'll go over the more relevant aspects of the bill as it now stands, both pros and cons, as well as ways to mitigate the effects of the latter.

First the good news

The SECURE Act contains many new provisions and changes to current legislation related to retirement readiness. Here are the more significant ones:

- **Removes IRA age limit** – Today, once you reach 70 ½, you can no longer contribute to an IRA, though you can contribute to a Roth IRA at any age, subject to income restrictions. The new law would allow for IRA contributions at any age.
- **Improves small business access to retirement plans** – A problem with small business retirement plans is that they are expensive to administer, and often the cost gets passed on to the participants in higher fees and lower returns. Small business owners also have the risk of fiduciary liability for the plans, a disincentive to offering them. The SECURE Act would permit multi-employer plans, helping reduce plan costs, and reduce the liability of the employer.
- **Increase the RMD age** – The age at which owners of tax-deferred investment account must start taking distributions is currently the year in which they turn 70 ½. The SECURE Act would increase the starting age for RMDs to 72; RESA has age 75 as its objective. This would permit extended tax deferral and eliminate the half-year birthday confusion.
- **Allow annuities in retirement plans** – Annuities are often referred to as "longevity insurance," as they provide a way to pool the risk of living too long and exhausting one's financial assets. Since 2015, deferred annuities called Qualified Longevity Annuity Contracts (QLACs) have been permissible within retirement plans, with limits on the amount that can be used with a QLAC. The new legislation will make it easier for employers to add a range of annuity options within their retirement plans, both deferred and immediate.
- **Plan eligibility for long-term part-time employees** – Yet one more way to increase the options for employee retirement plan participation.

Taken as a whole, the SECURE Act should give individuals more and better options for retirement savings and income. That's the good news. Now for the rest of the story.

The bad news: Say goodbye to "Stretch" IRAs

Congress needed a way to pay for this legislation, and what they came up with is the elimination of the "Stretch" IRA. Stretch IRAs, more properly called Inherited IRAs, currently permit tax-deferred retirement plans inherited by non-spouse beneficiaries to be withdrawn over their lifetimes, thus reducing yearly taxes and allowing for long-term tax-deferred asset growth. In the SECURE Act, any non-spouse inherited IRA will have to be emptied within 10 years after it is inherited.

The problem for children and other non-spouse beneficiaries is that they could potentially lose a large percentage of the inherited assets to taxes, particularly if they receive the inheritance during their peak earning years. I'll illustrate with an example. Let's say a parent dies today with $1 million in tax-deferred assets and has designated his or her 40-year old only child as sole beneficiary. Under current law, that child would only be required to take out $22,936 (2.3 percent of the plan value) the following year, and the amount would increase gradually as their life expectancy decreased and assets grew. Under the SECURE Act, they would be required to withdraw the full $1 million plus growth within 10 years. The tax on the additional income could possibly push the inheritor into a higher marginal tax bracket, thus paying out more of the withdrawal in taxes than they would have paid with a Stretch IRA. Woe to the child who waits until Year 10 to take out the full amount and gets hit with the tax bill for over $1 million in additional income that year. However, there are ways to mitigate this potential tax crisis.

Remedies for inherited asset tax angst

As with any change in tax legislation, the tax gurus have already come up with ways to reduce the tax damage to your heirs:

- **Roth conversions** – This is a taxable conversion of IRA assets into Roth IRA assets. I regularly recommend these to my clients as a way of reducing taxable income in their later retirement years by doing them during their lower income "gap years," typically after they retire but before their RMDs and Social Security kick in. Roth IRAs have no RMDs for original owners and are tax-free when withdrawn. The SECURE Act provides further incentive to do so, as the heirs would also withdraw money from their inherited Roth IRAs tax-free.
- **Charitable Remainder Trusts (CRTs)** – CRTs require that at least 10 percent of the assets in the trust eventually go to charities, but the income to the CRT beneficiaries can be stretched out over their lifetimes. The costs of setting up and administering a CRT can be considerable and should be compared to the taxes saved by this approach. This option tends to work best with qualified plans in excess of $1 million at the time of the owner's death. CRTs can be established during one's lifetime, or at death as testamentary trusts.
- **Life insurance** – Withdraw some of your assets in IRAs and use them to purchase life insurance placed in a trust for your beneficiaries. There is no tax on life insurance proceeds, and no RMDs to worry about.

These are the best current approaches. I'll be writing more on this subject once the SECURE Act becomes law.

George Gagliardi is a financial advisor with Coromandel Wealth Management in Lexington, where he helps clients develop and implement investment and retirement strategies. He can be reached at (781) 728-9001 or george@CoromandelWM.com. George is affiliated with Trust Advisory Group, Ltd., a Registered Investment Advisor. *This article is intended for general information purposes only, and may not be appropriate for your specific circumstances. Investment advice is particular to each individual, and should only be given after an individual situation has been reviewed.*