

Status report on the SECURE Act— and why those with substantial IRA assets are wary?

Saving for retirement is an important financial goal. IRAs, Roth, 401k plans and work-based retirement savings plans are powerful planning tools to contribute, defer taxes and manage retirement savings. Many clients are disciplined with their yearly contribution and will be able to accumulate enough for their golden years.

It is not uncommon for us to see wealthy individuals enter retirement with \$3 million or more in an IRA. Those funds are typically a combination of assets rolled over from 401(k) and other workplace plans plus gains on contributions made directly to IRAs over the years.

For many wealthy families, planning for IRA account disposition encompasses much more than using them as a source of current income during retirement years. Now, IRAs are often central components to estate plans. In some cases, their tax-advantaged status can be extended to benefit heirs.

This rise of high-balance IRAs—and sophisticated estate-planning practices associated with them—is the main reason why many wealthy families are watching the progress of the SECURE Act through Congress with a wary eye. The bill would eliminate the “Stretch IRA,” a popular planning tool wealthy families have used to transfer IRA balances to the next generation. In my view, there’s likely to be financial-planning solutions that can adequately deal with these issues. That’s a topic I’ll return to in future comments if the legislation progresses as anticipated.

But for now, let’s set the stage with a brief “status report” on the SECURE Act, focused primarily on how it might impact wealthy families’ estate-planning considerations.

What is it?

The U.S. House of Representatives passed the “Setting Every Community Up for Retirement Enhancement Act” on May 23, 2019. The bill passed with overwhelming bipartisan support—the vote tally was 417-3.

If the bill passes the Senate and is signed by the President, the impact of its more than 20 sections would be the most significant update to the retirement-saving landscape in many years.

Key provisions

The bill includes characteristics likely to appeal to large groups of people, such as:

- > Enabling long-term part-time employees to participate in 401(k) plans.
- > Allowing IRA contributions—to both Traditional and Roth accounts—as long as the contributor wishes. (At present, contributors must stop by age 70 ½, when current rules mandate Required Minimum Distributions (RMDs) to begin.)
- > Raising the RMD age threshold from 70 ½ to 72.
- > Permitting annuities to be among investment options in 401(k) plans—and modifying liability rules to make it more likely plan sponsors would include them.
- > Offering employers more substantial tax credits and other incentives if they offer retirement plans with automatic enrollment.
- > Increasing usability of 529 education-savings accounts, to accommodate their use for qualified student loan repayments of up to \$10,000 and apprenticeships.

Proposed Stretch IRA Limitations

In addition to the widely attractive provisions noted above, the SECURE Act also carries a provision that wealthy families may find much less attractive. The issue is that inherited IRAs must be distributed within 10 years of the inheritance date, with only a few exceptions including spouses and children who are either minors or who have disabilities.

This means the tax advantages of IRAs cannot be extended, or “stretched,” as some in the industry call it, for as many years when passing an IRA to non-spouse heirs, including adult children. (Under current law, those adult-child heirs would not have to start taking RMDs until they received age 70 ½.)

Without some careful planning, the elimination of the “stretch” characteristic of IRAs could upend core aspects of existing estate plans, especially in two cases:

- > Those with substantial amounts in their IRA accounts— amounts likely to endure past the subsequent death of a spousal heir, if any;
- > Those who have no spouse or are divorced and choose to name children directly as beneficiaries.

For people in these categories, new strategies will be needed. As I noted above, I expect attractive solutions to be available through careful planning. In the meantime, we’ll stay tuned to the legislative progress of the SECURE Act.

The House version of the bill would make these and other provisions law as of January 1, 2020. With that date now approaching and some uncertainty around when the Senate may take up the bill, any final law may carry a later start date. But even if the effective date is, say, a year later, individuals and families will do well to revisit key aspects of their IRA-related estate plans as soon as possible after the final shape of the law is known.

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Calamos Wealth Management 2020 Calamos Court | Naperville, IL 60563 | 888.857.7604 | www.calamos.com/wm | cwm@calamos.com
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