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## SECURE Act Impacts Estate Plans: Here's What to Know (Part I)

### SUMMARY

A new law, which is called “SECURE” (Setting Every Community Up for Retirement Enhancement), applies to retirement plans of people who die after December 31, 2019. Among the most important aspects of SECURE from an estate planning perspective is that in all but a few limited cases, it eliminates one of the most commonly used tax strategies that previously applied to tax deferred Individual Retirement Accounts and many other qualified retirement plans at the death of the IRA owner or plan participant: the ability to “stretch” withdrawals from the accounts over the lifetime of the beneficiary or beneficiaries of the plan. The elimination of this technique may force tax deferred assets to be withdrawn—and therefore taxes to be paid—much sooner. This could have a dramatic impact on estate planning for anyone with significant retirement accounts.

#### Retirement Planning Under Prior Law

In general, upon the death of an IRA owner or the participant of many qualified retirement plans prior to January 1, 2020, the designated beneficiary of the plan had three options. First, the beneficiary could withdraw all of the assets from the plan immediately. That would lead to the beneficiary's immediate enjoyment of the assets, but also to the immediate taxation (as ordinary income at the rates applicable to the beneficiary) of all of the assets withdrawn. Second, the designated beneficiary could withdraw the assets at any time before the end of the year which contained the fifth anniversary of the participant's death (known as the “5-year rule”), thereby deferring the tax for up to five years. Third, the designated beneficiary could withdraw the assets from the plan in installments based on the beneficiary's life expectancy and “stretch” the retirement assets and the taxes over the beneficiary's life expectancy.

Because of the significant tax benefit the stretch technique could provide, when permissible that was the most common selection. And, as retirement accounts often are a significant portion of a person's wealth, rather than keeping those accounts separate from the person's estate plan, planners advised various methods for incorporating the accounts into their clients' estate plans while ensuring that the stretch could still apply at the clients' deaths, primarily through the use of “see-through trusts” which could be either a “conduit trust” or an “accumulation trust.” These trusts contain special language and meet specific requirements under the tax laws that allow the oldest trust beneficiary to be considered the beneficiary of the retirement account for purposes of determining the required withdrawals from the account each year.

A conduit trust immediately passes out any retirement assets the trust receives to an identified beneficiary. The beneficiary of the conduit trust to whom the retirement assets must be distributed is considered the beneficiary of the retirement account, and, therefore, that beneficiary's life expectancy can be used to determine the minimum amount of the retirement account that must be withdrawn annually by the trust, subjected to income tax, and, ultimately, distributed to the identified beneficiary.

An accumulation trust allows the trustee to accumulate the assets of the trust, including any retirement assets received, for later distributions to one or more beneficiaries. In this case, the life expectancy of the oldest potential beneficiary would be used to determine the amount of tax deferred retirement accounts that must be withdrawn annually. Regardless, the potential stretch provided a substantial benefit, and these trusts were particularly useful for minor beneficiaries who should not receive immediate distributions.

## **SECURE Retirement Planning**

On some levels, SECURE allows for some tax deferral benefits compared to the previous law. Importantly, the IRA owner or plan participant herself does not need to start withdrawing assets from her retirement accounts until the end of the year in which she turns 72 (compared to 70.5 under prior law). Also, as long as there is a designated beneficiary of the plan, SECURE basically replaces the 5-year rule discussed above with a 10-year rule, and in cases where the 5-year rule would apply, the designated beneficiary now has until the end of the year which contains the tenth anniversary of the participant's death to withdraw all of the assets from the plan. When there is no designated beneficiary (including when retirement assets pass to the participant's estate, a charity, or a non see-through trust) the 5-year rule still applies.

However, those benefits are contrasted with a significant detriment, the almost complete elimination of the stretch for inherited retirement assets. Outside of a small class of "eligible designated beneficiaries" (the participant's surviving spouse, a minor child of the participant, a disabled beneficiary, a chronically ill beneficiary, or a beneficiary less than ten years younger than the participant), all designated beneficiaries are subject to the 10-year rule. In fact, even eligible designated beneficiaries ultimately can become subject to the 10-year rule. For example, while a minor child of the participant is an eligible designated beneficiary and can withdraw assets from a retirement account based on her own life expectancy, as soon as she attains the age of majority, the 10-year rule applies and the balance of the retirement assets must be withdrawn before the end of the year which contains the tenth anniversary of such date.

This change can have a dramatic impact on both existing estate plans and on the development of estate plans going forward. In the case of a conduit trust, for example, although a minor child of the participant may be the beneficiary of a conduit trust, the withdrawal of retirement assets no longer can be stretched over the beneficiary's lifetime. It also is important to note that only the participant's minor child (and not a grandchild or more remote descendant) may be an eligible designated beneficiary. In many cases, this will force the complete distribution of the retirement assets to the beneficiary within 10 years regardless of the participant's intent when the trust was created based on the law at that time.

Aside from special rules which could govern an accumulation trust of which a disabled beneficiary or a chronically ill beneficiary is the beneficiary, accumulation trusts no longer can qualify as eligible designated beneficiaries, and the 10-year rule automatically applies to such trusts. Retirement assets still can be retained in the trust (unlike a conduit trust) for the beneficiaries of the trust, which may be more in line with the participant's intent, but with a potential cost: significant tax, at the maximum income tax rate applicable to trusts, when the retirement assets must be distributed to the trust.

## **Estate Planning Considerations**

The implementation of SECURE could have a substantial impact on the estate plans of anyone with significant retirement assets and all such plans should be reviewed. Estate planning under SECURE will continue to include planning to defer income tax as long as possible. It also may include planning for the payment of the tax, including the source and the funding of the tax payment.

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