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THE SECURE ACT - THE GIFT THAT KEEPS ON GIVING

The 2019 holiday season brought a considerable gift for retirement savers, financial advisors and other professionals involved with the retirement savings industry. On December 20, 2019, the Setting Every Community Up for Retirement Enhancement Act of 2019 (the SECURE Act) was signed into law.[1] The SECURE Act changes many of the tax rules to expand retirement savings opportunities. These changes affect workers, retirees, beneficiaries, IRA owners, business owners, and retirement plan sponsors. With many details still being finalized by the IRS and Department of Labor (DOL), service providers will be working throughout 2020 to incorporate the rule changes into their operating systems, account owner communications, and reporting procedures.

These changes will provide financial advisors multiple opportunities throughout the coming year and beyond to engage in meaningful interactions with their clients and industry contacts regarding the impact of the new rules, and potentially create new relationships with prospects. Your account owner and business owner clients will need to be educated about the new savings enhancements. As service providers sort through the changes in operational requirements and deadlines, you have an opportunity to serve as a conduit to help your clients understand the impact of these new requirements. To take advantage of the gift that will keep on giving for years to come, financial advisors must first be certain they have a firm grasp of the rule changes and the impact the SECURE Act could have on their clients, prospects, and service providers.

THE PATH AND THE PURPOSE

The changes made by the SECURE Act to encourage saving for retirement have had strong support in Congress over the years. According to the U.S. Bureau of Labor Statistics, only 51% of private industry workers participate in a workplace retirement plan.[2] That percentage shrinks for those who work for small business employers; only 28% of businesses with fewer than 10 employees offer a retirement plan.[3] It has long been a policy initiative on both sides of the aisle to ease the burden and expense of sponsoring a retirement plan so more employers can offer retirement savings opportunities to their workers.

Legislative proposals dating back to 2015 have included many of the same retirement savings provisions that were ultimately passed in the

[1] Further Consolidated Appropriations Act, 2020, December 16, 2019, Division O – Setting Every Community Up for Retirement Enhancement (SECURE) Act, https://www.appropriations.senate.gov/imo/media/doc/H1865PLT_44.PDF
[2] U.S. Bureau of Labor Statistics, National Compensation Survey, March 2018, https://www.bls.gov/ncs/ebs/benefits/2018/ownership/private/table02a.htm
[3] SCORE.org, Press Release, "Owners Lack a Retirement Savings Plan, April 17, 2019, https://www.prnewswire.com/news-releases/one-third-of-small-business-owners-lack-a-retirement-savings-plan-300833644.html

SECURE Act. Yet the road to passage wasn't easy. In May 2019, the House passed its version of the SECURE Act almost unanimously (417-3). With bi-partisan support in Congress and broad support for the bill throughout the retirement industry, swift passage in the Senate was expected. But at least two Senators raised concerns about the bill and blocked a vote. One of the sticking points was a provision stricken from the House version that would have expanded the use of 529 plan assets. Despite general approval of the legislation, the bill was not brought to the floor for debate or vote throughout summer or fall of 2019. Numerous supporters from the retirement saving industry continued to advocate for the SECURE Act. With just days before the end of the year – and before many of the provisions were to become effective – Congress was able to attach the SECURE Act to a federal funding bill, the *Further Consolidated Appropriations Act, 2020*.[1]

The SECURE Act is designed to enhance retirement savings opportunities for individuals, encourage business owners to sponsor retirement plans, and provide more workers access to workplace savings plans. To increase retirement plan coverage for workers, many of the SECURE Act changes enhance incentives for employers to sponsor retirement plans and reduce some of the administrative burden to make sponsoring a plan easier. Other provisions are aimed at helping individuals save more – for longer – in retirement plans and IRAs. Most of these changes became effective as of January 1, 2020.

Individuals need to be educated about the changes, especially those age 70 or older, and the impact of the new rules on their financial and estate planning strategies. Businesses that already sponsor a retirement plan for their employees will need to make certain mandatory operational changes in 2020. They will also need to decide whether to incorporate any of the optional changes that will be available. Businesses that do not yet sponsor a retirement plan may find that some of the changes remove obstacles that prevented them from adopting a plan in the past.

This paper summarizes the changes included in the SECURE Act, focusing on the provisions that impact IRAs and IRA-based employer plans.

[1] Further Consolidated Appropriations Act, 2020, December 16, 2019, Division O – Setting Every Community Up for Retirement Enhancement (SECURE) Act, https://www.appropriations.senate.gov/imo/media/doc/H1865PLT_44.PDF

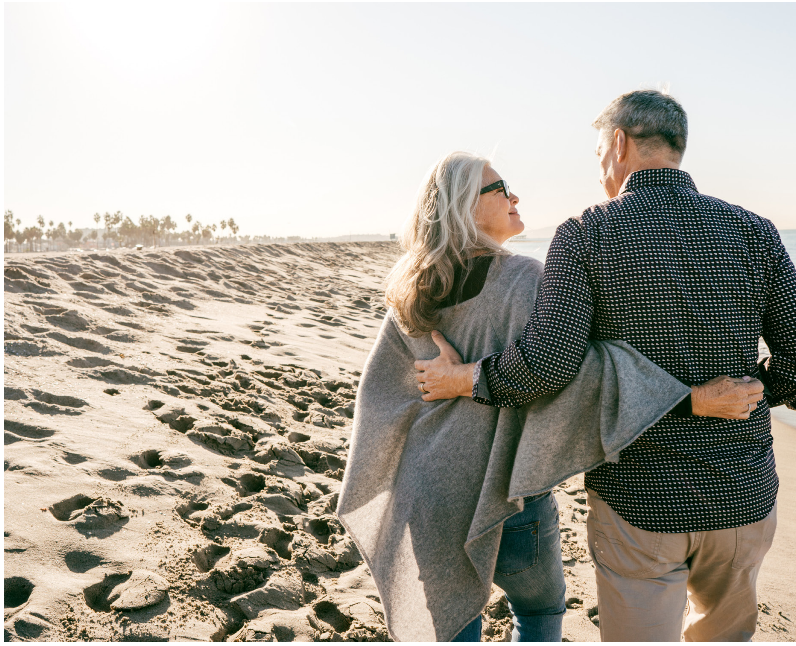
CHANGES AFFECTING IRAS, IRA OWNERS AND BENEFICIARIES

1: ELIMINATES AGE LIMIT ON IRA CONTRIBUTIONS – EFFECTIVE 1/1/2020

Before the Act, the IRA rules prohibited individuals from contributing to a Traditional IRA for the year they reached age 70½ and subsequent years.

After the Act, there is no longer an age limit on Traditional IRA contribution eligibility. Individuals can continue contributing to Traditional IRAs so long as they have earned income to support the contribution. For example, for 2020, IRA owners over age 50 may contribute up to $7,000 to their IRAs so long as they have $7,000 of earned income. If an IRA owner does not also participate in an employer-sponsored retirement plan, they will likely be able to deduct their Traditional IRA contributions.

The opportunity to make additional contributions is a reason for financial advisors to reach out and connect with their IRA clients. You can inform them of the option to continue making contributions as long as they have earned income, particularly those who are nearing age 70½. You may want to do this before the April 15 tax-filing deadline. You can also remind them what constitutes "earned income" for purposes of making IRA contributions. (IRS Publication 590 – A contains a list of "taxable compensation" that qualifies.) IRA owners age 70½ and older should also know that if they choose to make a Qualified Charitable Distribution, they must reduce the eligible QCD amount (maximum of $100,000 per year) by the amount they take as deductions for Traditional IRA contributions made after age 70½.



2: INCREASES RMD STARTING AGE – EFFECTIVE 1/1/2020

Before the Act, IRA owners had to begin taking a required minimum distribution (RMD) from their Traditional, SEP and SIMPLE IRAs for the year they turned age 70½. The deadline to take the RMD for the 70½ year was April 1 following the 70½ year.

After the Act, IRA owners are required to begin taking RMDs by April 1 following the year they reach age 72. This is effective for anyone who had not yet reached age 70½ by December 31, 2019. This means that anyone who did not reach age 70 by June 30, 2019, may wait until age 72 to begin taking RMDs from their IRAs. Those who had had reached age 70½ by the end of 2019 must continue taking RMDs.

The opportunity for advisors is to inform their clients that they may now have an additional two years to let their retirement savings continue growing tax-deferred before they are forced to begin taking taxable distributions. You may want to reach out especially to those who are nearing or just past age 70½ to help them understand how the change applies to them specifically, based on their birth date. The rules are confusing, and IRA owners may have already received a notice from their IRA custodian incorrectly informing them that an RMD is due for 2020. The IRS has issued guidance directing IRA custodians to correct any incorrect RMD notices by April 15, 2020, but you may want to inform them before that date to eliminate confusion. If they reached age 70½ before the end of 2019, they will need to keep taking their RMDs timely each year to avoid a 50% penalty tax.

Also note that the Treasury Department/IRS has proposed new life expectancy tables for calculating RMDs and beneficiary payments, but the new tables have not been finalized and cannot be used yet.

3: ELIMINATES BENEFICIARY PAYOUT OPTIONS – EFFECTIVE 1/1/2020

Before the Act, depending on the beneficiary's relationship to the IRA owner and the IRA owner's age at death, a beneficiary may have had some or all of the following payment options available:

- **Five-Year Rule –** take payments of any amount on any date as long as the IRA is depleted by the end of the fifth year following the IRA owner's death
- **Life Expectancy Payments –** take a minimum annual payment until the IRA is depleted

- **Transfer or Rollover to Own IRA –** move inherited IRA assets to spouse's own IRA or employer plan

After the Act, the payment options for spouse beneficiaries remain the same as they were before the Act. But most nonspouse beneficiaries will now be required to distribute all assets in an inherited account by the end of the tenth calendar year following the IRA owner's death, regardless of the IRA owner's age at death. This includes adult children of the IRA owner. Beneficiaries may choose to take any amount of payments during this time so long as the account is depleted by the end of the tenth year.

Certain types of beneficiaries are not subject to this rule and may continue to take distributions under the old rules. This includes beneficiaries who, as of the date of death, are a:

- Surviving spouse
- Disabled individual
- Chronically ill individual
- Minor child of the IRA owner (until they reach the age of majority in their state)
- Nonspouse beneficiary who is less than 10 years younger than the IRA owner

Beneficiaries who inherited retirement savings prior to 2020 may also continue to take beneficiary payments under the old rules.

The opportunity for advisors to consult with clients on how the elimination of the stretch IRA strategy might affect their estate plans or future inheritances could turn into much more than a single educational session. Most beneficiaries who are not married to the IRA owner at the time of death will lose the option to delay the tax liability and preserve the tax-deferred growth on inherited IRA assets for longer than 10 years. If a beneficiary subject to the 10-year rule dies before depleting the assets, a successor beneficiary will be required to deplete the remaining assets by the original 10-year deadline. Your IRA clients will need guidance and assistance in reviewing their beneficiary designations and evaluating the overall impact these rules will have on their estate plans. They may need to explore other options to achieve their goals for passing their savings on to their heirs. Further guidance and detail on the beneficiary distribution options will be coming from the IRS. You may have clients who have become beneficiaries by that point and will need help understanding their options and how to adjust long-term financial plans and manage the tax implications.

4: ADDS NEW EXCEPTION TO 10% EARLY DISTRIBUTION TAX – EFFECTIVE 1/1/2020

Before the Act, there was no distribution trigger or penalty exception allowing retirement savers younger than age 59½ to distribute retirement savings to help pay for birth or adoption expenses.

After the Act, IRA owners may take a distribution of up to $5,000 from their IRA, free from the 10% early distribution tax, to help pay for expenses of childbirth or adoption. An eligible adoptee is anyone other than a spouse's child, younger than age 18 or with special needs that render them incapable of supporting themselves. Distributions must be taken within one year of the child's birth or adoption. This change also applies to 401(k), 403(b), and governmental 457(b) plans as an optional distribution trigger if the plan elects to allow it. Individuals who take an IRA or plan distribution for this reason may repay the distribution to an IRA or the distributing plan.

→ **The opportunity** to access retirement savings may be welcome news for individuals who need help paying for childbirth or adoption expenses to avoid incurring debt. Most workers are not otherwise eligible to take a distribution from their employer's retirement plan while they are still employed, outside of a plan loan which must be repaid. IRA assets may be withdrawn at any time for any reason, but an exception to the 10% early distribution tax means more money in the parents' pockets. It appears that the $5,000 limit applies per individual, so each parent may take advantage of the distribution option for the same birth/adoption, for a total of $10,000.

In addition to educating clients about this new option, you may also take the opportunity to discuss ways they could save for similar expenses in a Health Savings Account (if eligible) or an emergency savings account. You may also want to discuss the negative effects of withdrawing assets from retirement savings if they cannot pay it back and how they could increase their retirement savings contributions in the future to make up for it.

IRS guidance is still needed to answer questions regarding reporting, accepting repayments, and implementing this distribution type into employer plan documents and processes, so follow-up communications with those who take advantage of this option may be needed.

CHANGES AFFECTING SMALL BUSINESS OWNERS

The SECURE Act specifically includes changes to benefit small employers (100 or fewer employees), which are intended to result in increased access to workplace retirement plans for more workers.

1: INCREASES TAX CREDITS FOR PLAN START-UP EXPENSES – EFFECTIVE 1/1/2020

Before the Act, small employers could take a tax credit for qualified start-up costs for establishing a SEP plan, SIMPLE IRA plan or qualified retirement plan. To be eligible, an employer must have 100 or fewer employees earning at least $5,000 per year. The plan must include at least one rank-and-file employee, and the employer cannot have maintained a qualified retirement plan during the three years preceding the first credit year. The tax credit was equal to 50% of the qualified start-up costs up to $1,000 for up to three years (i.e., up to $500 per year for three years).

After the Act, the eligibility requirements for small businesses to take a tax credit for plan start-up costs remain the same, but the amount of credit available is significantly increased.

A small employer may take a tax credit between $500 – $5,000 per year for three years. The credit is now calculated as 50% of plan start-up costs up to the lesser of a) $5,000 or b) $250 multiplied by the number of non-highly compensated employees eligible to participate in the plan (but at least $500).

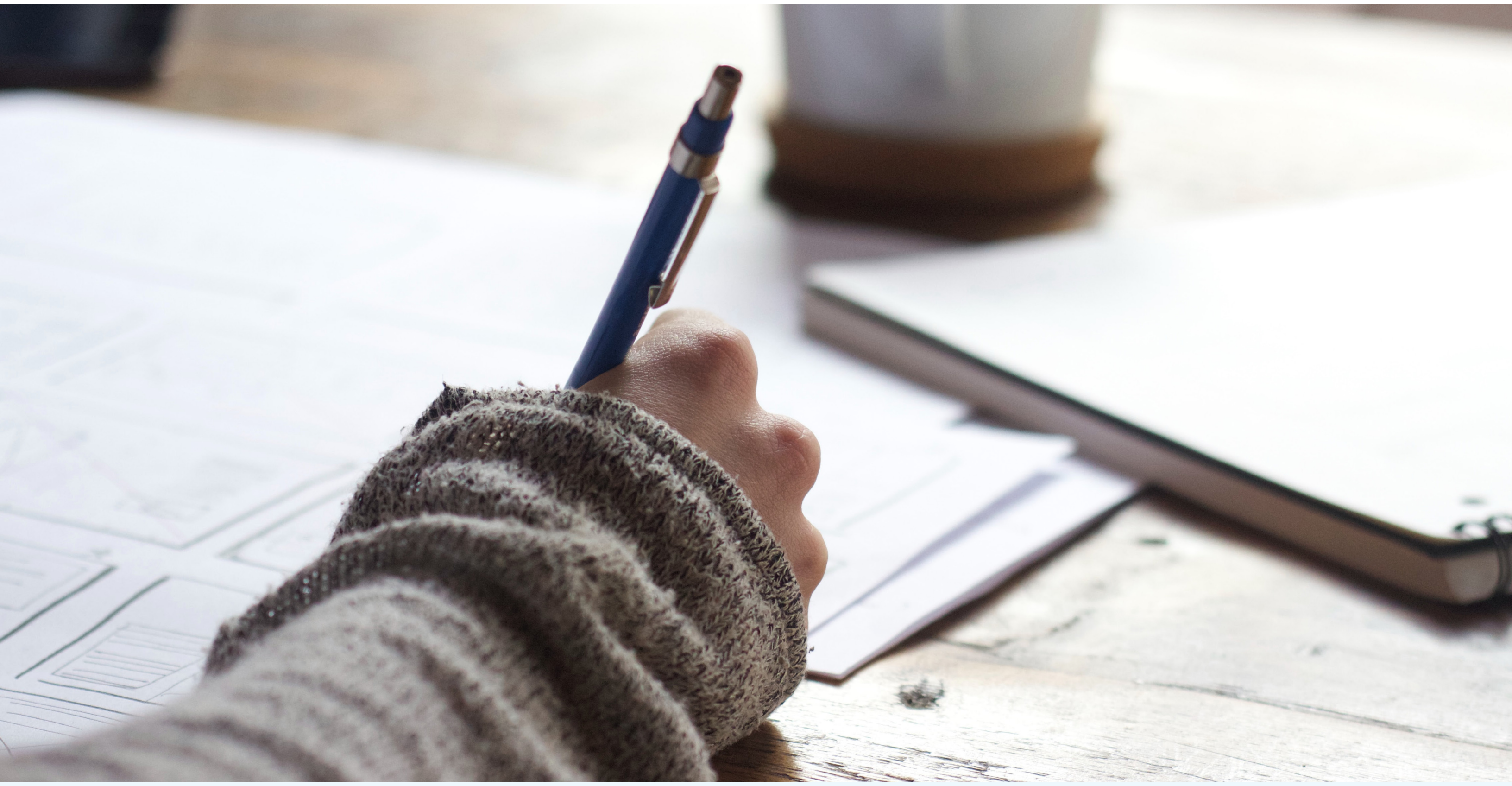
- **The opportunity** to offset much more of the initial plan start-up expenses with a tax credit may be especially helpful for some employers who had chosen not to establish a retirement plan previously because of the cost. As an advisor, use this opportunity to inform your small business plan prospects about the increased tax credit available for plan start-up costs and to educate them about the benefits of establishing a retirement plan. Make sure they know that the credit is available for expenses incurred in establishing and administering the plan and for providing plan information/ education to employees. You may also want to offer your services in assisting with employee education.

2: ADDS NEW TAX CREDIT FOR AUTOMATIC ENROLLMENT – EFFECTIVE 1/1/2020

Before the Act, there was no tax credit available to employers who added an automatic enrollment feature to their retirement plan.

After the Act, small businesses that add automatic enrollment to a new or existing 401(k) or SIMPLE IRA plan may claim a $500 per year tax credit for up to the first three years the automatic enrollment provision is in effect.

The opportunity for financial advisors is having yet another reason to contact small business plan prospects and existing small business plan clients. Once they understand that Congress is advocating for automatic enrollment for small business plans, more employers may take another look at adding an automatic enrollment feature to their SIMPLE IRA or 401(k) plan – especially since the credit offsets the costs for the first three years.



CHANGES AFFECTING EMPLOYER-SPONSORED RETIREMENT PLANS

The SECURE Act includes even more changes for employer-sponsored retirement plans than for IRAs. Most of the changes are intended to make it easier for employers to sponsor retirement plans for their workers.

Some of the changes will be optional for employers to include, others must be incorporated into plan operations this year or in years to come. IRS guidance is still needed to clarify details of the changes and to instruct plan sponsors as to how to incorporate the changes into administrative procedures and plan documents. Service providers, such as plan recordkeepers and third-party administrators, will be keeping a close eye out for this clarifying guidance to ensure plans maintain operational compliance and plan document compliance when plan amendment requirements are announced. (The amendment deadline will generally be December 31, 2022.)

The chart on page 11 includes many of the changes affecting employer-sponsored retirement plans made by the SECURE Act. Note that some of the changes are the same as those for IRAs or IRA-based plans. All these changes are effective as of January 1, 2020, for calendar-year based retirement plans, unless otherwise noted.

SUMMARY

The SECURE Act brings massive – and in some cases long-awaited – changes to IRAs and employer-sponsored retirement plans in an effort to encourage employers to sponsor retirement plans for their employees and to encourage individuals to save more for retirement. Almost all of your retirement savings clients and the service providers you work with will be affected by these changes. You have multiple opportunities to create touchpoints with clients and prospects to educate them about how these law changes will affect their retirement savings efforts and showcase your services.

SECURE Act Changes for Retirement Plans

Extends required minimum distribution (RMD) starting age to 72 for individuals who did not reach age 70½ in 2019 or earlier
Requires nonspouse beneficiaries to deplete accounts within 10 years for account owner deaths occurring after 2019, with exceptions for spouses, disabled or chronically individuals, children until the age of majority, and beneficiaries less than 10 years younger than the account owner
Increases small plan start-up tax credit and creates a new tax credit for small plans using automatic enrollment
Creates new distribution-triggering event and exception to the 10% early distribution tax for distributions of up to $5,000 taken to pay for childbirth and adoption expenses
Extends deadline for an employer to establish a qualified retirement plan until the business's tax-filing deadline, plus extensions (for employer contributions only)
Increases automatic escalation deferral cap for Qualified Automatic Contribution Arrangements (QACAs) from 10% to 15% after first year of participation
Eliminates safe harbor 401(k) notice requirement and extends time for employers to decide whether to adopt safe harbor status if providing a nonelective safe harbor contribution
Requires plans to allow "long-time, part-time" employees into the plan if they work at least 500 hours in 3 consecutive years – plans are to start counting hours as of January 1, 2021, so the first year these participants will enter the plan under this provision will be 2024
Creates new type of Multiple Employer Plan (MEP), called a Pooled Employer Plan (PEP), to allow unrelated employers to join a single plan administered by a Pooled Plan Provider (PPP) – effective January 1, 2021
Allows participants to roll over a lifetime income product to another plan or IRA if product is no longer available in the plan
Expands the fiduciary safe harbor for plan sponsors selecting lifetime income product providers for the plan
Requires plan sponsors to provide a lifetime income disclosure each year to show participants how much their account balance would generate in monthly payments in retirement – effective 12 months after Department of Labor issues guidance or model notice and assumptions
Increases IRS penalties for late filing of Form 5500 and 8955-SSA and failing to provide a withholding notice/election

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ABOUT US

STRATA Trust Company has quickly catapulted to become a premier national custodian for alternative assets and non-exchange traded investments in self-directed IRAs. STRATA has over $2 billion in assets under custody, and for over a decade has helped over 35,000 investors nationwide use their retirement account funds to invest.

With offices in Waco and Austin, Texas, our team's vast experience in handling the details and complexities that real estate transactions require is unrivaled. Our seasoned team's experience in the custody of alternative assets spans over 350 years. With a well-established reputation for honesty and integrity, STRATA is committed to delivering responsive, flexible and innovative solutions.

At STRATA, we work to ensure that the highest standards for safety and soundness are met. As a subsidiary of Horizon Bank, SSB, STRATA is a Texas-chartered trust company regulated by the Texas Department of Banking, which has long set the benchmark among state banking regulators. Strict controls are in place to ensure the safety of uninvested cash, and independent auditors are retained to conduct regular audits of our operations.