

Navigating SECURE Act 2.0's Impact on Estate Planning for Retirement Benefits

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IRAs and Qualified Retirement Accounts

- **Evolving Retirement Landscape**
 - **Increased longevity**
 - A 65-year-old can expect to live well into their 80s
 - Senior population expected to double over 30 years
 - **Retirement income sources have evolved**
 - Responsibility to save for retirement has been shifted to the employee
 - Increases in delayed retirement
 - **Trillions of dollars in IRAs and Qualified Plans**
 - Taxes must be considered when taking distributions
 - Consider: early withdrawal penalties, RMDs, distribution timing, etc.
 - BUT: only 56% of the adult population participates in workplace retirement plans. (US Bureau of Labor Statistics 2022)



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Distribution Planning for Retirement Benefits

- Rules have evolved over the last 70+ years:
 - 1950s Cash or Deferred Arrangement (CODA) profit sharing plans started to appear
 - 1974 Enactment of the Employee Retirement Income Security Act (ERISA)
 - 1978 The Revenue Act of 1978 created the foundation for the 401(k)
 - 1981 IRS Regulations clarified that a portion of payroll could be deferred to a 401(k)
 - 2001 EGTRA introduced the Roth 401(k)
 - 2020 SECURE Act extended Required Beginning Date to 72 and eliminated the “stretch” for Inherited IRAs
 - 2023 SECURE Act 2.0 and corresponding regulations made major changes to Required Beginning Dates, inherited IRA rules, and catch-up contribution limits



Distribution Planning for Retirement Benefits

- SECURE Act 2.0 – Overview of Selected Major Changes:
 - Employees automatically enrolled in new 401(k) and 403(b) plans
 - Employee deferrals auto-escalate (initial: 3%; 1% increase annually up to 10%- 15% max)
 - Employers may match qualified student loan payments as if elective deferrals
 - Required Beginning Date Age raised to 73 (plus staggered future increases)
 - Catch-up contributions beginning in 2025 are increased for 60, 61, 62, and 63 year olds
 - Reduced penalty for failure to take RMDs
 - Statute of Limitations for failure to take RMD is 3 years, triggered by the taxpayer's filing due date, with extensions (SOL used to be triggered by filing Form 5329 Additional Taxes on Qualified Plan form)
 - Expansion of exceptions to 10% early withdrawal penalty
 - 529 plan accounts can be transferred to the Beneficiary's Roth IRA (with limits)



Distribution Planning for Retirement Benefits

- **SECURE Act 2.0 – Overview of Selected Major Changes (related to Roth Accounts):**
 - There is no Required Beginning Date for Roth accounts, including employer Roth accounts
 - Employers may permit employees to elect that employer matching and non-elective contributions be made as Roth contributions
 - Employees making \$145,000 or more per year who make catch-up contributions to employer-sponsored retirement plans, like a 401(k), will have to instead put that money into Roth accounts (extended effective date of this provision to 2026)
 - *For now, ages 50 and older can continue to make catch-up contributions after 2023, regardless of income*



Distribution Planning for Retirement Benefits

1. **During Lifetime**
 - Pre-59 ½ considerations
 - Required Minimum Distributions (“RMDs”)
2. **After Death**
 - Beneficiary designations
 - Post-death RMDs
3. **Planning Considerations**
 - Inherited IRAs – control and access
 - Minors, special needs, 2nd marriages
 - Correcting inadvertent benefit distributions



During Lifetime

- Contributions are generally pre-tax and earnings are tax-deferred
- Income taxation on benefits is generally avoided until distributions are made
- Penalties:
 - Too Early Tax – 10% penalty on distributions received prior to age 59 ½
 - SECURE Act 2.0 expanded exceptions: terminal illness, domestic abuse, Federal disasters, personal and family emergency expenses, long-term care premiums
 - Too Late Tax – 25% penalty on the amount of a minimum distribution that is required to be distributed but is not
 - Prior to SECURE Act 2.0, penalty was 50%



During Lifetime

- **Required Minimum Distributions**
 - Once you reach the Required Beginning Date (“RBD”), you have to start taking RMDs:
 - First RMD must be taken by April 1st of the year after you turn the “Applicable Age”:
 - 2019 and earlier: 70 ½
 - 2020 to 2022: 72
 - 2023 to 2032: 73
 - 2033 forward: 75



During Lifetime

- **Required Minimum Distributions**

- **Examples:**

- Sally turns 73 on December 6, 2023. Her Required Beginning Date is April 1, 2024.
- Harry turns 73 on January 1, 2024. His Required Beginning Date is April 1, 2025.



During Lifetime

- **New Exception under SECURE Act 2.0:**

- There is no Required Beginning Date for Roth accounts, including employer Roth accounts.
- **If still working, RMDs can be delayed from employer accounts.**
 - RBD = April 1st of the year after retirement.



During Lifetime

- **Calculating the RMD:**
 - If Participant's spouse is the sole beneficiary and beneficiary is more than 10 years younger:
 - Use the Joint Life & Last Survivor Table
 - All other Participants:
 - Use the Uniform Life Table
 - For inherited IRA beneficiaries:
 - Use the Single Life Table



What Happens to IRA & Plan Balances at Death?

- **Key questions:**
 - Had the deceased owner started taking RMDs?
 - Whether Participant's death occurred Pre- or Post-RBD is important in determining what rules apply to the beneficiaries
 - Was the RMD satisfied for the Participant's year of death?
 - The Beneficiary's RMD requirements begin the year *after* death
 - Year of Death RMD must be taken by December 31st – decedent's RMD rules apply to year of death RMD calculation (not the beneficiary's RMD calculation)
 - If not taken by the decedent before death, it must be taken by the beneficiary (Rev. Ruling 2005-36)
 - Who/what is the account beneficiary?
 - Non-Designated Beneficiary – "5-Year Rule"
 - Estate, charities, and non-qualifying trusts
 - Designated Beneficiary – "10-Year Rule"
 - All other individual beneficiaries and qualifying trusts
 - Eligible Designated Beneficiary – "Stretch IRA"
 - Certain individual beneficiaries and certain qualifying trusts for those individuals



Post-Death

- **Beneficiary Designations**
 - Importance of proper beneficiary designations on IRAs and Qualified Plans
 - Avoid unintended consequences associated with:
 - Taxes
 - Creditor issues
 - Divorce/remarriage
 - Financial management concerns
 - Substance abuse concerns
 - Tailoring designations to accomplish objectives



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Post-Death - Non-Designated Beneficiary

- Applies to what beneficiary? Where none is listed, estate, charities, and certain qualifying trusts
- If Participant died before RBD:
 - “5-Year Rule” applies
 - Must empty account by the end of the 5th year following the year of the Participant's death (i.e., December 31st of the year that contains the 5th anniversary of the Participant's death)
 - No withdrawals required before the end of that 5th year
- If Participant died after RBD:
 - “At least as Rapidly Rule” applies
 - Beneficiary must take annual RMDs based on deceased Participant's age in the year of death using the Single Life Table, with no recalculation each year



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Case Study: Joe with no beneficiary listed

- Joe named his wife Mary as beneficiary of his IRA in 2005. He was in a hurry and told his benefits coordinator that he would get back to them about a contingent beneficiary. And, of course, he never did.
- Mary died unexpectedly, and Joe was too distraught to engage in sound financial planning.
- Joe died in 2023 at age 78 with \$500K left in his IRA. What happens?
 - No beneficiary listed, then the default rule is that the estate is the beneficiary
 - Year of death RMD? Must be satisfied if not already taken
 - Died after RBD; see Single Life Table for 78 year old: 12.6 is the Applicable Denominator
 - 2024 RMD: (12.6 minus 1) = 11.6; RMD is 1 divided by 11.6, or 8.62% of the prior year-end balance
 - 2025 RMD: (12.6 minus 2) = 10.6; RMD is 1 divided by 10.6, or 9.43% of the prior year-end balance
 - And continuing in the same fashion each year until Zero balance
- Is that the end of the story?
 - IRAs are governed by contract, and some agreements may provide for a beneficiary if blank (e.g., spouse, issue, per stirpes, etc.)
 - Coordinate with IRA custodian to have separate shares established so each beneficiary can pull out their portion over the required timeframe



Post-Death - Designated Beneficiary

- Applies to what Beneficiaries? Most individuals and non-qualifying trusts
- If Participant died before RBD:
 - “10-Year Rule” applies
 - Must empty account by the end of the 10th year following the year of the Participant’s death (i.e., December 31st of the year that contains the 10th anniversary of the Participant’s death)
 - BUT no withdrawals required before the end of that 10th year
- If Participant died after RBD:
 - “10-Year Rule” applies
 - For years 1 through 9, Beneficiary’s annual RMD based on the longer of:
 - Beneficiary’s Single Life Table life expectancy vs. Participant’s Single Life Table life expectancy
 - Must empty account by the end of the 10th year following the year of the Participant’s death (i.e., December 31st of the year that contains the 10th anniversary of the Participant’s death)



Case Study: Mary with a Designated Beneficiary

- Mary (55) dies on May 1, 2024 with a \$3 million IRA. She already satisfied her 2024 RMD. Mary's nondisabled son, Barry (25), is designated as sole beneficiary of the IRA.
 - Barry's has until December 31, 2034 to empty the inherited IRA
- Mary (85) dies on May 1, 2024 with a \$3 million IRA. She already satisfied her 2024 RMD. Mary's nondisabled son, Barry (55), is designated as sole beneficiary of the IRA.
 - Single Life Table for 55 year old: 31.6 is the Applicable Denominator
 - 2025 RMD: $(31.6 \text{ minus } 1) = 30.6$; RMD: 1 divided by 30.6, or 3.27% of the prior year-end balance
 - 2026 RMD: $(31.6 \text{ minus } 2) = 29.6$; RMD: 1 divided by 29.6, or 3.38% of the prior year-end balance
 - And continuing in the same fashion for the 2033 RMD (Year 9)
 - Barry must empty the inherited IRA by December 31, 2034



Post-Death - Designated Beneficiary

- **When do the inherited IRA RMD rules go into effect?**
 - **IRS Notice 2023-54:**
 - **For Designated Beneficiaries: No annual RMDs required in 2021, 2022, and 2023**
 - **A Designated Beneficiary who took an RMD in 2021, 2022, and/or 2023 can retribute the withdrawn amount by September 30, 2023**



Post-Death – Eligible Designated Beneficiary

- **Applies to what Beneficiaries?**
 - Participant's surviving spouse
 - Participant's minor child
 - Disabled or chronically ill beneficiaries
 - Beneficiaries not more than 10 years younger than the participant



Post-Death – Eligible Designated Beneficiary

- **Spousal beneficiaries**
 - (1) Spousal rollover into an IRA in surviving spouse's name
 - (2) Treat as their own IRA
 - (3) Elect to be Treated as the Deceased Participant
 - (4) Stretch IRA



Case Study: Surviving Spouse

- Maude (55) dies in 2023 with a \$3 million IRA. Maude designated her spouse, Harold (53), as sole beneficiary of the IRA.
- Harold's options:
 - (1) Spousal rollover
 - Roll over the retirement account balance into Harold's own IRA
 - Harold is the owner and subject to same rules as all participants (RBD, RMD, etc.)
 - (2) Treat as his own IRA (almost the same as a rollover)
 - Must elect this treatment by the later of: (i) December 31 of the year after the date of death, or (ii) year Harold turns 73
 - (3) Elect to be treated as the Deceased Participant
 - Harold can delay RMDs until Maude would have reached 73
 - Most beneficial when surviving spouse is older than the deceased Participant
 - Clarification needed from IRS to determine how to make election and whose birthdate is used to calculate RMDs
 - (4) Stretch IRA:
 - Death Before RBD: Harold's RMD beginning in 2024 based on Single Life Table with recalculation
 - Death After RBD: RMDs based on the longer of Harold or Maude's life expectancy



Post-Death – Eligible Designated Beneficiary

- **Participant's Minor Child**
 - **Modified "Stretch IRA" applies**
 - **Until age 21, the minor child must receive annual RMDs based on child's Single Life Table life expectancy**
 - **Once age 21, the 10-year rule kicks in, RMDs continue, and the account must be emptied by the end of the year the child reaches age 31**



Post-Death – Eligible Designated Beneficiary

- Chronically ill or disabled beneficiary as of date of Participant's death
 - Measured at date of death only; illness/disability occurring after Participant's death doesn't count
- If Participant died before RBD:
 - "Stretch IRA" rule applies
 - Beneficiary must receive annual RMDs based on beneficiary's Single Life Table life expectancy
- If Participant died after RBD:
 - "Stretch IRA" with "Longer of" variation
 - Beneficiary must receive annual RMDs based on the life expectancy of the Beneficiary or the Participant, whichever is longer



Post-Death – Eligible Designated Beneficiary

- Beneficiaries not more than 10 years younger than the Participant
- If Participant died before RBD:
 - "Stretch IRA" rule applies
 - Beneficiary must receive annual RMDs based on beneficiary's Single Life Table life expectancy
- If Participant died after RBD:
 - "Stretch IRA" with "Longer of" variation
 - Beneficiary must receive annual RMDs based on the life expectancy of the Beneficiary or the Participant, whichever is longer



Post-Death – Multiple Beneficiaries

- **Multiple beneficiaries can complicate the timing and amount of RMDs received by all beneficiaries**
 - **In general**: Must use the life expectancy of the oldest designated beneficiary (exceptions where the beneficiary mix includes trusts, minor children, or disabled/chronically ill beneficiaries)
 - **Example**: Darlene names her brother (75) and child (40) as equal beneficiaries of her IRA. Darlene dies in 2023. 12/31/23 account balance of \$500,000. What is the amount of beneficiaries' first required distribution?
 - Use brother's life factor (age 76 in 2023) = $(14.1-1)=13.1$; 7.63% RMD
 - Brother's share = \$19,083.97 ; child's share = \$19,083.97
 - BUT, they should just establish separate shares to avoid this issue



Post-Death – Multiple Beneficiaries

- **In most cases, the multiple beneficiary rule can be avoided by complying with the “Separate Share Rule”**
 - **Deadline**: Count remaining beneficiaries as of September 30th of the year following the Participant's death (“Beneficiary Finalization Date” or “BFD”)
 - **A beneficiary who establishes a separate inherited IRA account by the BFD has the RMD rules apply to the beneficiary individually (not the group of beneficiaries)**
 - **Prior example**: If separate accounts were timely completed in prior example, child's 2024 RMD is \$5,707.76 (versus \$19,083.97)



Post-Death – Trusts as Beneficiaries

- **Example: Marge (40) dies in 2023 naming her Revocable Trust as beneficiary of her \$1 million 401(k) account. Trust directs division of assets among separate trust shares for each of Marge's three minor children.**
- **How are the 401(k) benefits handled?**
 - **Trusts are considered non-designated beneficiaries (5-Year Rule) unless:**
 - **The Trust qualifies as a "see-through trust" and**
 - **All of the countable beneficiaries are individuals**



Post-Death – Trusts as Beneficiaries

- **See-Through Trust: (Four-parts)**
 - (1) Trust is valid under State law
 - (2) Irrevocable
 - (3) Documentation is provided to the plan administrator by October 31st of the year following death
 - (4) All the trust beneficiaries who have a beneficial interest in the retirement benefits held by the Trust are identifiable
- **If the Trust passes this test, and the countable beneficiaries are all individuals, then the Trust qualifies as a Designated Beneficiary or Eligible Designated Beneficiary (depending on the beneficiary composition). Otherwise, the 5-Year Rule applies.**



Post-Death – Trusts as Beneficiaries

- **Trust Considerations**
 - **Who are the trust beneficiaries?**
 - If individuals, are they all Eligible Designated Beneficiaries? What distribution standard applies?
 - If charities, when do charities receive their share?
 - **Is the trust a see-through Conduit Trust?**
 - Trust that requires all retirement benefit distributions must be paid to or for the benefit of the specified beneficiary
 - **Is the trust a see-through Accumulation Trust?**
 - Any see-through trust that isn't a Conduit Trust



Case Study: Minor beneficiaries

Jerry and Elaine are married, in their 30s, and have four minor kids. If they both pass away, they are concerned about how to designate their IRA/401(k) assets.

- **Avoid naming minor as direct beneficiary**
- **Conduit trust?**
- **Accumulation trust?**
- **Non-see-through trust?**



Case Study: Surviving Spouse (Children from a prior relationship)

- Dennis has a \$2 million IRA and is married to Delores (Dennis's 3rd marriage). Dennis and Delores each have children from prior marriages. Dennis wants to provide for Delores but wants his kids to benefit after Delores passes away.
- Options:
 - (1) Designate Delores as direct beneficiary?
 - **Problem: What if Delores names her children from a prior marriage? Or her new husband?**
 - (2) Name a Conduit Trust for Delores's benefit?
 - **Delores must be the sole trust beneficiary**
 - **Trustee is required to pass out to Delores all distributions the trust receives from the inherited IRA**
 - **If Delores lives to her life expectancy, almost all benefits will have been paid out to her**
 - (3) Name an Accumulation Trust for Delores's benefit?
 - **All benefits will be paid and taxed to the trust at trust rates, except to the extent distributions are passed out to Delores**
 - (4) Name a Charitable Remainder Trust?
 - **CRT pays no tax on the lump sum payout of the IRA, can provide for a unitrust stream of income to be paid out during spouse's lifetime**
 - **On the death of the surviving child, all remaining CRT funds pass to charities**
 - **Produces a charitable deduction to estate**



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