



Sunday, February 9, 2020

Client Conversations

In this issue we explore the new Setting Every Community Up for Retirement Enhancement (SECURE) Act and how it may affect your benefit planning, along with how some early retirees may have a unique window of opportunity to take advantage of Roth conversions.

Q: I've just heard about the SECURE Act. What does it mean for retirees?

A: If you're just hearing about the Setting Every Community Up for Retirement Enhancement (SECURE) Act of 2019 now, you're not alone. As a part of the government's spending bill, Congress passed—and the president signed into law—this significant piece of retirement legislation late in December as the holidays were kicking into high gear. And while the headlines at the time were focused on other, more sensational issues, the SECURE Act quietly brought about the most comprehensive changes to the U.S. retirement system in more than a decade.

Among the more than two dozen provisions contained in the SECURE Act are several that directly affect individual retirement account (IRA) holders, including:

- Pushing back required minimum distributions (RMDs) from IRAs and 401(k)s from age 70 1/2 to 72. Previously, IRA and 401(k) account holders were required to begin taking required distributions based on life expectancy from their accounts starting in the year that they turned 70 1/2. The SECURE Act delays the age at which retirement account holders must take RMDs to 72. That means that those not inclined to take distributions can push back both their distributions and the resulting tax consequences a bit longer.
- Eliminating the age cap for IRA contributions. Prior to passage of the SECURE Act, Americans weren't allowed to make IRA contributions after age 70 1/2—even if they had earned income. The SECURE Act eliminates the age cap to allow continued tax-deferred savings in recognition of increasing life expectancies and longer working lives.
- Forcing faster withdrawals from inherited IRAs. The new legislation still allows spouses to treat an inherited account as if it belonged to them. However, non-spouses must take a full payout

from an inherited IRA within 10 years of the original account holder's death. This provision eliminates the stretch IRA, a popular tax and estate planning concept, for the heirs of account holders who die in 2020 and later.

- Penalty-free distributions for birth or adoption. The SECURE Act allows IRA account holders to take up to a \$5,000 distribution penalty-free as a "qualified birth or adoption distribution" within one year of the birth or adoption.

The changes brought about by the SECURE Act will create tax-saving opportunities or complications for many Americans, so you should seek the advice of your tax and financial advisors, who can guide you based upon your personal facts and circumstances.

Q: I have just retired. Does it still make sense for me to do a Roth conversion?

A: Since you have just retired, it may make sense for you to convert some of your traditional IRA or retirement plan savings to a Roth IRA, depending on where your income is coming from and your effective tax rate. First a little background.

Introduced in 1997, the Roth IRA is a retirement savings vehicle that allows for contributions to be made on an after-tax basis. While these contributions to a Roth IRA are not tax-deductible, if you meet certain conditions, withdrawals from a Roth IRA are income tax-free, including both contributions and investment earnings. And unlike a traditional IRA, the Roth IRA rules do not force you to take required minimum distributions (RMDs) every year after you reach age 72 (formerly 70 1/2), so your money can stay in the account and keep growing tax-free—for you or for your heirs. These unique characteristics make Roth IRAs a potent financial planning tool.

Roth IRA contributions are limited based upon a taxpayer's modified adjusted gross income, but Internal Revenue Service rules allow the conversion of some or all of a traditional IRA or pre-tax balance in an employer-sponsored plan—like a 401(k), 403(b), or 457 plan—to a Roth IRA. A Roth conversion is typically a taxable event, so you will pay income tax on the conversion amount. That's an instant turn-off to some people but demands a closer look.

Because recent retirees cease having income from work, may not yet be receiving Social Security benefits, and aren't yet required to take required minimum distributions (RMDs) from their IRAs and retirement plan balances, they may find themselves in a low tax bracket—sometimes significantly lower than when they were working. This is especially true for those retirees who are withdrawing living expenses from their taxable accounts early in retirement.

If this sounds like your situation, now might be a good time. But you've got to be careful; a Roth conversion could actually bump you into a higher marginal tax bracket for the year you convert—potentially undoing some of the benefit. The good news is that conversions can typically be made over a several-year window, so you can manage how much you convert to take advantage of the lower tax bracket. The latter part of the year is generally the best time to do a Roth conversion so that you have a good idea of what your income—and tax rate—will be for the year. If this sounds complicated, it is. It's important to get it right because Roth conversions can't be undone, and the merits are highly dependent upon your unique financial circumstances. That's why you should always consult with your financial and tax advisors before undertaking a strategy like this to make sure it is right for you.

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