Tax Changes 2019 – IRAs and Retirement Plan Issues

Part of the "Further Consolidated Appropriations Act, 2020" includes various tax changes. We previously sent an email regarding the Extenders portion of this new law. Today's email is on another part titled the Setting Every Community Up for Retirement Enhancement Act of 2019 (SECURE Act of 2019) and involves IRAs and retirement plans. Here are the sections of the SECURE Act that we feel will likely impact a majority of our readers. ALL OF THESE PROVISIONS ARE EFFECTIVE FOR TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 2019, UNLESS SPECIFICALLY STATED OTHERWISE.

- RMD age is increased to age 72 instead of the former age 70.5. This provision applies to taxpayers who attain age 70.5 after December 31, 2019. In other words, taxpayers who reach age 70.5 during 2019 or before must continue taking their RMDs in 2020 and after.

– Repeal of Maximum Age for Traditional IRA Contributions. Taxpayers can now make contributions to a traditional IRA without regard to an age limitation (formerly contributions were not allowed for any year in which the taxpayer was age 70 or older by the end of the year).

In connection with the age repeal, any taxpayer who makes a Qualified Charitable Distribution (QCD) must reduce the QCD exclusion by all deductible contributions to a traditional IRA made for all years ending on or after the year the taxpayer reaches age 70.5 (but not taking into account any deductible IRA contribution already used to reduce a QCD). The point of this connection is to prevent taxpayers from avoiding the requirement to take charitable contributions on Schedule A, while getting a tax deduction for the IRA contribution. Remember this reduction only applies in connection with deductible IRA contribution for years on or after the taxpayer reaches age 70.5.

Example 1: Grandpa has a traditional IRA worth $50,000 made up of contribution he made when he was in his 60s. At age 73 Grandpa deducts $6,000 contributed into his traditional IRA. At age 74, Grandpa makes a QCD of $4,000. Grandpa's QCD exclusion is limited to $0, meaning the entire $4,000 of QCD is NOT excludible from income. ($4,000 QCD less $6,000 deductible contributions to a traditional IRA after reaching age 70.5, but not less than $0). This leaves $2,000 of deductible traditional IRA contributions Grandpa has made since the year he reached age 70.5 to reduce the QCD in the future.

Example 2: Continuing with the above example, at age 75, Grandpa make no contributions to a traditional IRA but makes a QCD of $7,000. Grandpa's QCD exclusion is limited to $5,000 ($7,000 QCD less the remaining $2,000 of deductible contributions to a traditional IRA after reaching age 70.5).

- RMDs for Inherited Defined Contribution Plans (including IRAs) have changed to eliminate the so-called "stretch IRAs". The entire balance of the inherited account must now be distributed within 10 years after the year of the owner's death except in the case

of a “designated eligible beneficiary” (see below). In the case of an eligible designated beneficiary, the entire remaining balance of the inherited account must now be distributed within 10 years after the year of the designated beneficiary’s death. This provision applies to deaths taking place after December 31, 2019, except in the case of a government plan where this provision applies to deaths taking place after December 31, 2021.

A designated eligible beneficiary includes:
a) The owner’s spouse,
b) A child of the owner who has not reached the age of majority, [this person shall cease to be a “designated eligible beneficiary” as of the year this person reaches the age of majority, with the remaining balance required to be distributed within 10 years of such year.]
c) A disabled person,
d) A chronically ill individual,
e) An individual not described above who is not more than 10 years younger than the employee.

- Nontaxable Difficulty of Care Payments are compensation for making IRA contributions.

– Certain Taxable Non-Tuition Fellowships and Stipend Payments Treated as Compensation for IRA Purposes. This provision only applies to amounts received that were to aid the taxpayer in the pursuit of graduate or postdoctoral study.

- A new exception to the 10% early distribution penalty permits withdrawals of up to $5,000 to be taken from an IRA or qualified retirement plan with respect to the birth or adoption of a child. The distribution must be made during the 1-year period beginning on the date on which the child is born or on which the legal adoption is finalized.

An adopted child must either:
1) Not have attained age 18, or
2) Must be physically or mentally incapable of self-support.

These distributions can also be rolled over to avoid taxation, with such rollover being treated as a trustee-trustee transfer.

- Expansion of Section 529 Plans and qualified expenses. Now the normal expenses for fees, books, supplies, and equipment required for participation in an apprenticeship program certified and registered with the Secretary of Labor. This provision is effective for taxable years beginning after December 31, 2018.

Also included in qualified expenses for Section 529 plan distributions is the repayment of an education loan up to $10,000 lifetime maximum. This includes the repayment of an education loan of the taxpayer OR a sibling. Each student has one $10,000 maximum. Any amount of loan repaid for a sibling uses up part of that sibling’s $10,000 maximum,

so it will be important for siblings to keep track of how much of this lifetime maximum has been used up each year. This tracking is kind of like the American Opportunity Credit tracking of the "per student" amount. This provision is effective for taxable years beginning after December 31, 2018.

- The minimum penalty for not filing found in Section 6651(a) is increased from $330 to $435, effective for returns DUE AFTER December 31, 2019.

- Kiddie tax computation reverts back to the old method, requiring information about the parents' and siblings' returns instead of the simplified method the TCJA gave of using the trust tax rates. This provision (Section 501) is affective for taxable years beginning after December 31, 2019. HOWEVER, a taxpayer can elect to have this provision apply to ANY taxable years beginning after December 31, 2017 (i.e., to 2018, 2019, or both). The details of this election will be provided by IRS.

There are other sections of the SECURE Act we did not include above such as:
- Increase in Credit Limitation for Small Employer Pension Plan Startup Costs
- Qualified Cash or Deferred Arrangements Must Allow Long-Term Employees Working More than 500 but Less Than 1,000 Hours per Year to Participate
- Plan Adopted by Filing Due Date for Year May be Treated as In Effect as of Close of Year
- Benefits Provided to Volunteer Firefighters and Emergency Medical Responders

A copy of the entire Act can be found at congress.gov and clicking on Public Laws and then choosing the "Further Consolidated Appropriations Act, 2020 (Public Law 116-94)". The SECURE Act provisions can be found in Division O.

Other tax issues such as the repeal of the medical excise tax and Cadillac tax (Division N) and extenders & disaster relief (Taxpayers Certainty & Disaster Tax Relief Act of 2019 found in Division Q) are included in this same document.

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