Distribution planning under the SECURE Act

The SECURE Act (Setting Every Community Up for Retirement Enhancement Act of 2019) changes the way inherited retirement accounts are distributed, requiring most non-spouse beneficiaries to fully distribute account balances within ten years after the death of the owner. This is referred to as the "ten-year rule" and is a stark difference from the "stretch" option, which allowed beneficiaries to distribute inherited retirement accounts gradually, based on their remaining life expectancy. Given these new rules, here are some key factors to consider when distributing inherited retirement accounts.

Some beneficiaries can still stretch distributions based on life expectancy

The SECURE Act creates a new definition for certain account beneficiaries — referred to as "Eligible Designated Beneficiaries" (EDBs). These beneficiaries are still eligible for life expectancy payouts:

- Spouses
- Disabled or chronically ill beneficiaries
- Minor children of the account owner (until reaching age 21 when the 10-year rule applies)
- Beneficiaries not more than ten years younger than the deceased account owner

Named beneficiaries who do not meet one of these requirements are simply referred to as "designated beneficiaries" and include most non-spouse heirs. There may be instances where no beneficiary is named, or the estate or certain (non-qualified) trust is designated as the beneficiary of the account. These rarer occurrences are referred to as "non-designated beneficiaries." Depending on the circumstances, following the death of the owner, these accounts may have to be distributed within five years.

The ten-year rule applies to inherited accounts where the owner died after 2019

Existing "stretch" distributions where the owner passed away prior to 2020 are grandfathered. However, if the existing beneficiary dies before the account is exhausted, the 10-year rule applies to successor beneficiaries. Additionally, the ten-year rule applies to retirement plans and IRAs, including Roth IRAs.

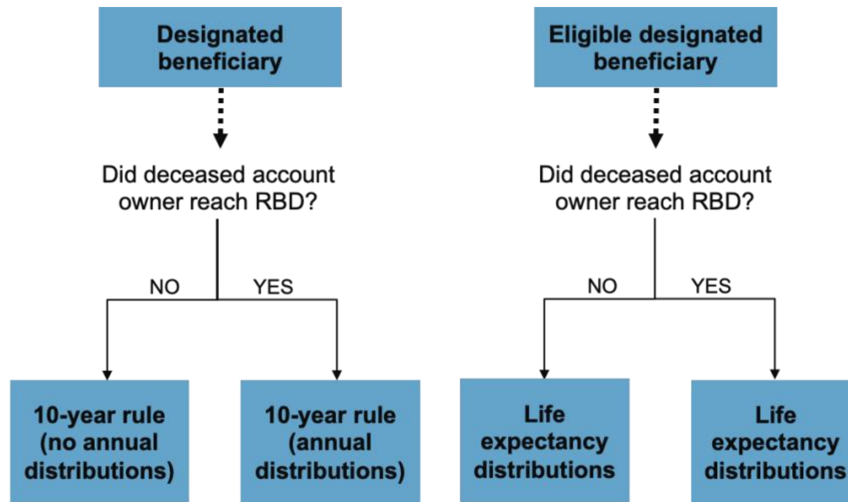
Trust arrangements may also be subject to the 10-year rule

Prior to the SECURE Act, if the trust met several requirements and qualified as a "see-through" trust, the option to stretch distributions based on the life expectancy of beneficiaries was available. Generally, under the new rules, unless trust beneficiaries are EDBs the 10-year rule applies.

Proposed regulations may change the way the ten-year rule applies

For heirs subject to the 10-year rule, initial interpretation of the legislation suggested that no annual distributions were required. The only requirement was to fully distribute the account by the end of the tenth year following the year of death of the owner. However, the Treasury Department recently released proposed regulations on required minimum distributions. The latest guidance states that if the account owner died *after the required beginning date (RBD)*, the beneficiary would have to take annual distributions based on their life expectancy for the first nine years, followed by full distribution of the account in the 10th year. These are proposed regulations and subject to change.

Summary: How distributions apply under the SECURE Act rules



Sources: Based on proposed Treasury regulations subject to change. Setting Every Community Up for Retirement Enhancement Act of 2019; Treasury Department, Required Minimum Distributions, Notice of proposed rulemaking and notice of public hearing, REG–105954–20. Required beginning date (RBD) is generally April 1 of the year following the calendar year in which the account owner reaches age 73. In the case of an account owner dying after RBD, designated beneficiaries and eligible designated beneficiaries may opt to base annual distributions on the remaining life expectancy of the deceased account owner. Spousal beneficiaries have the option of rolling over an inherited IRA into their own IRA. While minor children of account owners are eligible for life expectancy distributions, once age of majority (21) is reached the 10-year rule applies. Eligible Designated Beneficiaries can opt to base distributions on the 10-year rule if desired, provided the original account owner died prior to reaching the Required Beginning Date (RBD).

Planning considerations for account owners and heirs

Since the new 10-year rule may result in retirement account balances being distributed sooner than anticipated, that may lead to unintended income tax issues for beneficiaries. Here are some potential considerations:

- Account owners may want to leave other assets to higher-income heirs, leaving retirement funds to beneficiaries in lower, or moderate, income tax brackets
- Account owners may consider spending down (or converting to a Roth) retirement funds while living, depending on their tax circumstances
- For those over the age of 70 ½ qualified charitable distributions (QCDs) may be a tax-efficient method of drawing down IRA funds while satisfying charitable wishes
- Retirement account heirs will want to time taxable distributions from inherited accounts over the 10-year period in conjunction with their personal tax situation
- If possible, heirs of Roth accounts may wish to wait until the last year of the 10-year period before distributing the account, allowing for potential tax-free growth over that period

Not FDIC insured | May lose value | No bank guarantee

For informational purposes only. Not an investment recommendation.

This information is not meant as tax or legal advice. Please consult with the appropriate tax or legal professional regarding your particular circumstances before making any investment decisions. Putnam does not provide tax or legal advice.

Putnam Retail Management

Putnam Investments | 100 Federal Street | Boston, MA 02110 | putnam.com II1002 AD2429675 9/22