2020 Individual Retirement Account Changes

The Setting Every Community Up for Retirement Enhancement ("SECURE") Act and the Coronavirus Aid, Relief, and Economic Security ("CARES") Act, both recently signed into law, are intended to help Americans save more for retirement and provide relief for individuals affected by the coronavirus (COVID-19) pandemic.

Following is a summary of the major IRA provisions:

SECURE ACT

Designed to help expand retirement savings options and preserve retirement income.

Age restriction eliminated

Starting in 2020, taxpayers with earned income may make contributions to traditional IRAs at any age. Previously, traditional IRA contributions could no longer be made starting in the year the taxpayer reached age 70½.

This SECURE Act provision is effective for 2020 and later tax years and is not retroactive. This means IRA owners age 70½ or older in 2019 cannot make prior-year contributions for 2019 in 2020, as they fall under the old eligibility rule.

This change brings the rules for traditional IRAs more in line with Roth IRAs, which have never had an age restriction for making contributions.

Payout provision

Starting with IRA owner deaths in 2020, most nonspouse beneficiaries who are more than 10 years younger than the IRA owner must distribute their inherited IRA assets within 10 years of the IRA owner's death.

Previously, these beneficiaries could take payments from their inherited IRAs over their own life expectancies, which meant that beneficiaries in their 20s and 30s could stretch out their payments (and the taxes due on them) for 50 or more years.

There are exceptions to the 10-year payout rule for beneficiaries who, at the time of the IRA owner's death, are:

- Married to the IRA owner
- Disabled
- Chronically ill
- No more than 10 years younger than the IRA owner
- Minor children of the IRA owner
- Recipients of certain annuitized payments begun before enactment of the SECURE Act

The exception for the IRA owner's minor children does not apply to minor beneficiaries who are not the IRA owner's own children. Once the IRA owner's minor children reach the age of majority, they must switch to the 10-year payout period.

This 10-year payout provision applies to distributions from traditional IRAs, Roth IRAs, and savings incentive match plan for employees of small employers (SIMPLE) IRAs. It also is not retroactive, so the beneficiary payment options for IRA owner deaths in 2019 or earlier remain unchanged.

Required minimum distributions
The SECURE Act increased the age at which required minimum distributions ("RMDs") from traditional IRAs and SIMPLE IRAs must begin from 70½ to 72. This provision is effective for distributions required to be taken in 2020 and later years by IRA owners who reach age 70½ in 2020 and later years.

This provision also is not retroactive, so IRA owners who reached age 70½ in 2019, and have already begun taking their RMDs, must continue to take them.

However, these IRA owners are not required to take RMDs in 2020 because the CARES Act waives all 2020 RMDs.

Penalty-free withdrawal exception
The SECURE Act now permits penalty-free IRA withdrawals for the birth or adoption of a child.

A "qualified birth or adoption" distribution is exempt from the 10% early distribution penalty tax (if applicable) for distributions of up to $5,000 in aggregate from IRAs and defined contribution retirement plans, 403(b) plans, and governmental 457(b) plans, per individual.

The $5,000 limit applies separately to each birth or adoption. A qualified adoptee is anyone (other than a child of the taxpayer's spouse) under age 18 or an individual who is incapable of self-support.

"Qualified birth or adoption" distributions may be repaid at a later date as rollover contributions to IRAs and eligible retirement plans (other than defined benefit plans).

IRA contributions by graduate students
Effective for 2020 and later years, certain stipends, fellowships, and similar payments to graduate and postdoctoral students will be treated as eligible compensation for IRA contribution purposes.

Previously, because some of these types of payments were not considered eligible compensation, graduate students were not able to make IRA contributions unless they had compensation from other sources.

Difficulty of care payments
Like graduate students, certain foster care providers also receive payments that are not taxable income and, as a result, may not have been able to make IRA contributions unless they have compensation from other sources.

Under the SECURE Act, these "difficulty of care" payments may increase the amount of nondeductible IRA contributions they can make (but not above the annual statutory limit).

<u>CARES ACT</u>
Designed to help Americans affected by the COVID-19 pandemic to both access retirement funds in cases of financial hardship and preserve retirement income by deferring RMDs and allowing repayments of coronavirus related distributions ("CRDs").

1. Waiver of 2020 RMDs. The CARES Act waives 2020 RMDs from traditional IRAs, simplified employee pension (SEP) IRAs, and SIMPLE IRAs. IRA owners, including beneficiaries, will not be required to take a 2020

RMD from their IRAs or inherited IRAs.

The RMD waiver also applies to IRA owners who reached age 70½ in 2019 but did not take their RMD before Jan. 1, 2020. This means that IRA owners who reached age 70½ and chose to delay their payment until April 1, 2020, will not have to take their 2019 or 2020 RMD.

RMDs are not eligible for rollover. However, IRA owners who took a distribution in 2020—before the CARES Act was passed—may be able to roll over the distribution, but only if it is within 60 days of receipt of the distribution and all of the other rollover requirements are met.

In addition, for IRA beneficiaries, 2020 is disregarded for purposes of the “five-year” rule for beneficiary distributions when IRA owners died before their required beginning date. Instead, one year is added to the five-year period.

For example, if an IRA owner died in 2018, the assets in the inherited IRA must now be distributed by Dec. 31, 2024, instead of by Dec. 31, 2023.

It’s important to note that the new “10 year” rule for noneligible designated beneficiaries under the SECURE Act is not affected by this CARES Act provision. The “10 year” period applies only to certain beneficiaries for deaths in 2020 or later years.

If an IRA owner dies in 2020, the “10 year” period would not start until 2021, the year after the year of the IRA owner’s death.

2. Penalty-free withdrawal exception for CRDs. The CARES Act creates a penalty-free withdrawal exception for coronavirus-related distributions (CRDs). The provision allows IRA owners to withdraw up to $100,000 in aggregate from IRAs and qualified retirement plans (e.g., a 401(k) plan, 403(b) plan, governmental 457(b) plan)—without paying the 10% early distribution penalty tax (if applicable)—and repay those amounts to an IRA or eligible retirement plan.

A CRD is a distribution made on or after Jan. 1, 2020, and before Dec. 31, 2020, to a qualified individual. A qualified individual is:

- Someone (or the spouse or dependent of that person) who is diagnosed with COVID-19 or the SARS-CoV-2 virus in an approved test, or
- A person who experiences adverse financial consequences as a result of being quarantined.

This can include being furloughed, laid off, or having work hours reduced due for a variety of factors determined by the Treasury secretary, including lack of child care or the closing or reduced hours of a business.

CRDs, while penalty-free, are still taxable to the IRA owner. But they are taxed ratably over a three-year period—rather than in the year of distribution—unless the IRA owner elects otherwise.

To help preserve retirement income, IRA owners may repay CRDs over a three-year period, beginning with the day following the day the CRD is made to an IRA or eligible retirement plan.

Repayments may be made in single or multiple contributions, and if made within the three-year period will be treated as satisfying the 60-day rollover requirement.

Extended 2019 tax-filing & IRA contribution deadline

Separate from the SECURE and CARES Acts, the IRS also extended the deadline to make 2019 IRA contributions.

IRS Notice 2020-18, issued March 20, 2020, extended the 2019 tax-filing deadline from April 15, 2020, to July 15, 2020, but did not address the IRA contribution deadline.

The IRS subsequently updated the Frequently Asked Questions on its website to confirm that the deadline for making IRA contributions also has been extended by three-months, from April 15, 2020, to July 15, 2020.

The SECURE Act and CARES Act have brought major changes to IRAs, and more changes are likely, especially in light of the coronavirus pandemic