# 2024 White Paper

# Have You Updated Your Retirement Legacy Plan?

## The SECURE Act, the IRS, SECURE 2.0 Act, and new provisions taking effect in 2024 bring major changes that can affect your current plan.

## The record stock market values at the end of 2023 means larger RMDs for many. The clock is ticking, and potentially future higher taxes may be looming.

## The stretch IRA was eliminated for many beneficiaries. In addition, the IRS has made beneficiary distributions more complicated.

**What now?**
**Protect yourself and your loved ones with planning options that can create better tax and estate plans for your retirement savings.**

**By Ed Slott, CPA**
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The SECURE Act (Setting Every Community Up for Retirement Enhancement) eliminated the stretch IRA for many beneficiaries. This has been in effect since 2020 and it could have a significant negative tax impact on the plans you've made for your retirement savings. The IRS and the SECURE 2.0 Act have added more complexity to retirement distributions for families. It's getting more difficult for you and your beneficiaries to avoid tax landmines when withdrawing retirement funds.



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RMDs (required minimum distributions) have become increasingly complex, especially for your beneficiaries who can be subject to several different RMD requirements depending on what kind of beneficiary they are and when they inherited.

There is also confusion as to when IRA owners must begin RMDs. That's because SECURE 2.0 raised the RMD age from 72 to 73, but only for those who turned 72 in 2023 (those born in 1951) or later. Anyone who turned age 72 in 2022,had to continue RMDs on their existing schedule. (See the section later discussing which age IRA owners will use as the beginning date for taking RMDs.)

The point here is that RMDs have become overly complicated to attempt on your own. Mistakes can be made, and some of them may not be fixable, so you have to get this right the first time. This is where your agents and financial advisors can be a welcome source of help.

While the tax and RMD rules seem to get more difficult to decipher each year, there are alternative solutions that can put your beneficiaries in a better position, providing them with larger inheritances and fewer taxes and allowing you to assert more control. One of the best options is to use cash value life insurance in place of a traditional stretch IRA. I call it *"The Life Insurance Replacement Plan,"* and that is the focus of this guide. You'll also see how many retirement tax provisions have changed in just the last few years, bringing added layers of complexity. This is yet another reason to look for simplicity, stability, and certainty with a life insurance policy as a potential complement to the traditional retirement and estate plan. Each year's tax changes continue to make this life insurance plan a more valuable component of your family's financial plan.

**Elimination of the Stretch IRA**

The so-called *"stretch IRA"* is never mentioned in the tax code. It is simply a term that has evolved over many years to describe the extended tax deferral available to beneficiaries of retirement plans, like your children and grandchildren.

However, beginning with deaths in 2020, Congress eliminated the stretch option for many beneficiaries and replaced it with a 10-year payout.

The 10-year rule requires accounts to be emptied by the end of the tenth year following the year of death.



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Does the 10-year rule apply to all beneficiaries? Not quite. There are five classes of so-called ***"eligible designated beneficiaries"*** who are exempt from the 10-year post-death payout rule and can still stretch RMDs over their life expectancy. However, this group includes only spouses and a limited group of non-spouse beneficiaries.

**IRS RMD Surprise for Beneficiaries – More Withdrawals May Be Required**
The 10-year rule on its surface seemed simple. But in February 2022, the IRS issued proposed regulations that made this more complicated for many beneficiaries. These IRS proposed regulations are the current rules as of this writing – in January 2024 - even though they are "proposed" at this point.
The RMD rules depend on when the beneficiary inherited (under the SECURE Act or not), what type of beneficiary they are, and in some cases, whether the IRA owner they inherited from died after the owner had already begun RMDs.

When the SECURE Act was enacted, it was widely believed that the 10-year rule had no annual RMDs, except at the end of the 10-year term when the full balance had to be withdrawn. However, in February 2022, the IRS surprised most of us by ruling that beneficiaries subject to the 10-year rule also will have to take RMDs for years 1-9 if they inherited from someone who had already begun taking their RMDs (meaning they died after their required beginning date (RBD)).

This created even more confusion, especially for beneficiaries who in 2022 found out that they were supposed to take an RMD in 2021.

Due to the confusion created by the IRS proposed regulations, in October 2022, the IRS said that affected beneficiaries would not be subject to the 50% penalty for missed 2021 and 2022 RMDs. This essentially meant that these RMDs did not have to be taken.

Then, in July 2023, the IRS once again had to waive the RMD penalty for 2023 for beneficiaries subject to RMDs for years 1-9 of the 10-year term.

**New Spousal Beneficiary RMD Rules for 2024**



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Since a spouse is overwhelmingly the most common beneficiary, it’s important to be aware of changes Congress made to spousal beneficiary options. These provisions were included in SECURE 2.0, but are not effective until 2024.

The most common option for a spouse beneficiary is to do a spousal rollover to the spouse’s own IRA. That provision is unaffected by the new provisions of SECURE 2.0. The spousal rollover is still available and advisable for most spouses who inherit an IRA or company plan account from their spouse. Of course there are exceptions and that is where you should seek advice to see which option is best for you. This is especially true since a spousal rollover is irrevocable. Secure 2.0 provides an alternative to a spousal rollover of an inherited retirement account by permitting the surviving spouse (if the sole designated beneficiary) to elect to be treated as a deceased employee for RMD purposes beginning in 2024.

The RMD rule changes mostly affect the less common situations where there is a large age difference between the spouses (i.e., when a younger spouse inherits from a much older spouse or when an older spouse inherits from a much younger spouse.) If you fall into these less common categories, there are RMD elections you may need to make. If this situation applies to you, definitely seek advice from your tax and financial advisors before selecting your RMD options.

All of these recent RMD complications are yet another reason why IRAs have become poor assets to leave to beneficiaries for wealth transfer or estate planning purposes. And they are another sign that alternative solutions, such as Roth IRAs and (assuming there is a protection need) life insurance, now warrants a closer look. This is especially true for those with larger IRA balances, since it is likely that more of those funds will be left to beneficiaries who may be saddled with all these complex RMD rules. This could lead to costly penalties and higher taxes.

**The Roth IRA Advantage**

One bright spot is Roth IRAs. Under the IRS regulations, those who inherit a Roth IRA enjoy special RMD advantages. The 10-year rule applies, but there are no annual RMDs for years 1-9 for inherited Roth IRAs, regardless of how old the Roth IRA owner was at death.

Under the tax rules, anyone who inherits a Roth IRA is considered to inherit from someone who died ***before*** reaching their RMD required beginning date (since Roth



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IRA owners are not subject to lifetime RMDs). So, the only RMD would be the full inherited Roth IRA balance that must be withdrawn by the end of the 10th year after death.

The Roth IRA tax advantage is that beneficiaries can hold the inherited Roth IRA funds for the full 10-year term accumulating tax free. When the Roth funds are withdrawn, they will all be income tax free to the Roth IRA beneficiaries. This is a big advantage that inherited Roth IRAs have over traditional inherited IRAs.

**SECURE 2.0 Act – Enacted December 29, 2022**

SECURE 2.0 did not address or correct the 10-year rule RMD issue requiring annual RMDs in years 1-9 when the IRA owner died after starting RMDs. So, it is likely that the IRS will keep this rule in place when they issue final regulations. As of this writing (January 2024), we are still waiting for final guidance from IRS. Keep in contact with your agents and financial advisors for the latest updates.

**RMD Penalty Lowered**

SECURE 2.0 reduced the 50% penalty for not taking an RMD to 25%. In addition, under current law, you may reduce the penalty to only 10% by correcting any shortfall in a timely manner (generally within two years after the year of the shortfall). However, the 50% RMD penalty was rarely assessed by IRS, likely due to the harshness of that penalty. The IRS was very liberal in waiving the penalty when someone missed an RMD, as long as that person filed Form 5329 with a reasonable explanation (RMD confusion, health issues, death in the family, incorrect advice, etc…) and they made up the missed RMD.

However, now that the RMD penalty can be as low as 10%, it's not clear if the IRS will still be as generous in waiving the penalty. The IRS has informally said that it will at least continue to entertain RMD waivers through Form 5329 filings. But in case the IRS hardens its stance, anyone subject to RMDs (plan participants, IRA owners and beneficiaries) should be more vigilant than ever to make sure that the correct RMD is timely taken.

**RMD Age Increased**

SECURE 2.0 has increased the RMD age from 72 (under the original SECURE Act) to age 73 in 2023, and to age 75 ten years later in 2033.



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This transition from age 72 to 73 to 75 may also cause some confusion, so the easy way to know which RMD age applies is to use this simple guide based on the year you were born:

Use age 72 –if you were born between July 1, 1949 and December 31, 1950 (use age 70 ½ if born before July 1, 1949)
Use age 73 – if you were born in 1951 – 1959
Use age 75 – if you were born in 1960 or later

One advantage of raising the RMD age is that you have another year to do more planning, like Roth conversions and life insurance options (detailed below) before the constraints of RMDs begin.

Roth conversions will be more expensive once RMDs begin. This does not mean that once RMDs begin that you can no longer convert your IRA to a Roth IRA, because you can. The issue is that the RMD amount must be withdrawn first, and that RMDs cannot be converted to a Roth IRA. You must first satisfy the RMD and pay the tax on those funds. Once that is done, then you can convert part or all the remaining IRA balance for that year. But this makes the Roth conversion more expensive tax-wise since you must first withdraw your RMD before being able to convert.

**2024 RMD Surprise!**

The stock market reached all-time highs at the end of 2023. That's great news for investors of course, but it also means that 2024 RMDs will be higher for many because required distributions are based on higher account values at December 31, 2023. For older IRA owners who may already have larger RMDs due to age, the 2024 RMD will likely be higher due to both age and 2023 year-end market values (especially if IRAs are invested in the stock market).

For Roth IRA owners, the stock market increase means the 2023 appreciation will generally be income tax free, plus Roth IRAs are not subject to lifetime RMDs. Roth IRA beneficiaries will also benefit from the income tax free accumulation. As discussed earlier, most Roth IRA beneficiaries who inherit in 2020 or later (under the SECURE Act) will still have to empty their inherited Roth accounts by the end of the 10th year after death, but they are not subject to any annual RMDs before then. So, those heirs can continue to take advantage of the tax-free growth until the end of the 10 years These tax benefits for Roth IRA beneficiaries are yet another



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reason you may want to consider converting your IRA to a Roth IRA now while tax rates remain relatively low for most.

**RMD Delay May Increase Taxes Later**

The increased RMD age provision may initially seem like a tax advantage. But a closer look shows that delaying RMDs can result in higher taxes later since ultimately the funds in the account will need to come out. Based on a higher account balance and a shorter life expectancy, future RMDs will likely be larger. To avoid this, consider strategic distribution planning before RMDs are required, in order to take advantage of historically low tax rates. Roth conversions and life insurance could be good long-term alternatives to taxable retirement account funds.

(Remember that the delayed RMD age won't help everyone. If you are already subject to RMDs under the old 70 ½ or 72 RMD age rules, you must continue to follow your existing RMD schedule.)

**RMD Mindset Planning**
**Think "Maximum," Not "Minimum"**

The "M" in RMD stands for "minimum." It does not mean "maximum." Most people generally focus on what the minimum amount is that they must distribute from their IRAs and other retirement plans. But given our low tax rate environment, expanding even further for 2024 and 2025, that may be the wrong way to think about RMDs.

Why wait until withdrawals *must* be taken?
Why take only the minimum required?

Consider changing your "minimum" mindset and think "maximum." In other words: How much can be withdrawn at the lowest tax rates? Using a "minimum" mindset takes control out of your hands and turns it over to the government's RMD schedule. It's usually best to take control of your IRA distributions to allow possibly larger tax savings for the rest of your lives, and beyond to your beneficiaries. Better planning can put you in control of your tax brackets.

Remember that the tax law now has a finite window of when most retirement funds must be withdrawn. Under the SECURE Act, most beneficiaries will have to fully



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withdraw these funds within 10 years after death. With these shortened windows, more retirement assets could be bunched into a higher tax bracket, which could leave you and your heirs with less, especially in cases where your beneficiaries may be in their own highest earnings years. Large RMDs from inherited IRAs can push them into even higher tax brackets, lessening the amount they can actually keep after taxes.

**Pre-RMDs (Required Minimum Distributions)**
Although RMDs for most IRA owners will have to start at age 73, why wait until then? Even if you are years away from when RMDs must begin, it might pay to take "pre-RMDs." This is especially beneficial if you can get some of those funds out at the low 2024 and 2025 rates, before those rates are scheduled to increase (assuming the Tax Cuts and Jobs Act reductions are not extended).

This strategy may not be for everyone. For example, some people may be in their highest earnings years and already at the top 37% tax rate. But even for those people, their future tax rates in retirement and their beneficiary's rates during the 10-year payout period could potentially be higher if more income is pushed into a shorter time span. If you wait, and only take the minimum beginning when you must at age 73, then more will be left to beneficiaries who will likely have to withdraw all those inherited IRA funds within a decade after death. The tax at that point could be substantial.

The key planning point here is to smooth out (and lower) the overall taxes that will have to be paid on these funds both during your life and in the 10 years after death by your beneficiaries. Under current tax law, there may only be three years left to do that before tax rates are scheduled to increase.

It's understandable that you might not want to withdraw because you either don't need the funds or don't want to pay a tax that could otherwise be deferred. However, make sure you understand that, considering our national financial woes with record debt and deficits, it's likely that taxes will have to increase at some point. Your retirement funds could likely be withdrawn at lower rates now and put to better use through potentially tax-free vehicles like Roth IRAs and life insurance. These funds could then begin to grow tax free, removing the uncertainty of future tax increases for both you and your beneficiaries.

**RMD Planning for Beneficiaries Subject to the 10-Year Rule**



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As discussed earlier, beneficiaries subject to the 10-year rule who inherited from someone who died after RMDs had begun must continue RMDs for years 1-9 of the 10-year term. For these beneficiaries, instead of having a very large final RMD in year 10, consider increasing distributions above the RMD in years 1-9 to smooth out the tax bill over the 10-year period. And beneficiaries subject to the 10-year who don't have annual RMDs in years 1-9 should nonetheless consider distributions during those years to avoid a big balloon distribution in year 10.

**Note:** IRA beneficiaries cannot convert their inherited IRA funds to Roth IRAs, but they can use those withdrawals for life insurance or other planning vehicles.

## Expanded Tax Brackets for 2024

Consider taking advantage of these historically low rates, which due to inflation have been lowered even further by expanded tax brackets.

**Taxable Income Brackets for 2024 *Ordinary* Income Tax Rates**

| Marginal Tax Rate | Married Filing Joint | Single |
|---|---|---|
| 10% | $0 – $23,200 | $0 – $11,600 |
| 12% | $23,201 – $94,300 | $11,601 – $47,150 |
| 22% | $94,301 – $201,050 | $47,151 – $100,525 |
| 24% | $201,051 – $383,900 | $100,526 – $191,950 |
| 32% | $383,901 – $487,450 | $191,951 – $243,725 |
| 35% | $487,451 – $731,200 | $243,726 – $609,350 |
| 37%* | Over $731,200 | Over $609,350 |

* The top rate is effectively 40.8% for those subject to the 3.8% Medicare surtax on net investment income (those with MAGI over the thresholds of $250,000 joint filers/$200,000 single filers).

These low rates are slated to end after 2025 (assuming no change in the law) and retreat to the higher pre-2018 levels.



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## SECURE 2.0 Act – Other Provisions of Note

### Qualified Charitable Distributions (QCDs) Expanded

There is good news if you are charitably inclined, have an IRA, and are age 70 ½ or older. Starting in 2023, a one-time only, $50,000 qualified charitable distribution (QCD) can be made to a charitable gift annuity, charitable remainder unitrust, or charitable remainder annuity trust. Although it is not clear, the $50,000 amount may be included in the annual $100,000 limit for "regular" QCDs.

Also, the QCD limit of $100,000 is indexed for inflation starting in 2024, thereby allowing you to move more money tax-free from your IRA to the qualifying charities of your choice. The 2024 limit has increased to $105,000. The 2024 $50,000 limit for charitable gift annuities and charitable remainder trusts has increased to $53,000.

## IRA Annuity Benefits are Expanded

### Larger Limits for Longevity Annuities with Qualified Longevity Annuity Contracts (QLACs)

The SECURE 2.0 Act repealed the 25%-of-assets limit for purchasing a qualified longevity annuity contract (QLAC) and increased the QLAC dollar limit. Now, up to $200,000 can be used from an IRA or plan account balance for such a purchase. This provision was effective for 2023. (Although the $200,000 limit is indexed for inflation, it remains $200,000 for 2024.)

If you are concerned about outliving your retirement savings, this change may help you better guarantee an income stream for later years. It also has the side benefit of reducing current RMDs.

### Income Annuities

Income annuities within a plan or IRA can now offer additional benefits *without violating any RMD rules*. Annuity benefits and options now allowed include guaranteed increases (up to 5%), lump-sum payments, accelerated payments and return-of-premium death benefits.

### Annuity Payments are Allowed to Be Aggregated with Other IRA Assets for RMDs


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SECURE 2.0 also changed the rules for aggregation of RMDs from IRAs by allowing aggregation of RMDs from annuitized IRAs. While this may be good news for certain IRA owners, hurdles and unknowns remain.

Historically, when an IRA owner was subject to lifetime RMDs, he could not aggregate an annuitized annuity payment with his other IRA balances. The annuity payment **was the RMD for that specific annuity only,** regardless if the payment was more than what would be required if the standard IRA RMD calculation was performed on that annuity. Oftentimes this led to frustration as IRA owners were required to take more money from their IRAs versus other IRA owners of the same age with similar balances, but who did not have annuities.

Effective for 2023, any "overage" from an annuity payment can be aggregated with RMDs from all other IRAs. Additionally, it appears SECURE 2.0 would also extend the ability to aggregate annuitized RMDs to situations where an individual has multiple IRA accounts, both annuitized and not.

### One Big Implementation Question

However, an annual valuation of the annuity is required to properly calculate the total RMD. Without a true valuation, a calculation is impossible. How would anyone know what the prior year-end IRA balance was to divide their life expectancy factor into? ***SECURE 2.0 does not elaborate on how this valuation is to be determined.***

Determining the annual value of the annuity could take different forms. For example, an actuarial present-value calculation might work. Or, existing regulations addressing how to value an annuity prior to a Roth conversion might be used. Regardless, since annuity valuation can be extremely complex, an official valuation from the annuity provider would seem to be the safest and most accurate way forward. Until an official valuation is received, any "overage payment" from the annuity provider cannot be safely aggregated with other IRA assets in order to calculate a total RMD.

### Expanded Roth Retirement Account Opportunities

Are you ready for more retirement savings opportunities with Roth IRAs? Congress opened the door to more Roth possibilities in its search for immediate tax revenue.



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In 2023, SEP and SIMPLE plans were allowed to include Roth contributions. Also, plans can allow employer matching contributions to be made on a Roth basis.

**Company Plan Catch-up Contribution Rule is Delayed by IRS Until 2026**
Under SECURE 2.0, beginning in 2024, all plan catch-up contributions for age 50-or-over higher-income employees *mus*t be Roth contributions. But due to implementation issues, IRS delayed this provision. It now will not be effective until 2026.

This means that high-income employees (per the law, this means employees whose wages from the company for the prior year exceeded $145,000), still have the option of having the catch-up contributions go to either the pre-tax 401(k) or the Roth 401(k) (if offered under the plan).

**Rollovers from 529 Plans to Roth IRAs**
SECURE 2.0 allows limited rollovers from 529 plans to Roth IRAs. This provision is effective in 2024.

Did your child earn a scholarship? Did the beneficiary of a 529 education account decide not to go to college and now there are funds remaining in the account? If you had concerns about what to do with funds left over in a 529 plan, this may be a good strategy to employ. Leftover 529 funds can now be rolled over to a Roth IRA in the name of the 529 beneficiary. However, there are restrictions. For example, the 529 plan must have been in place for 15 years, annual rollovers cannot exceed the annual Roth IRA contribution limit, and total lifetime rollovers cannot exceed $35,000.

**More Catch-up Contributions**
If you are nearing retirement, SECURE 2.0 brings more savings opportunities. Starting in 2025, individuals who are ages 60, 61, 62 and 63 will be eligible to make larger age 50-or-older catch-up contributions to their work plans. Also, the IRA catch-up contribution limit, which has been stuck at $1,000, will be indexed for inflation beginning in 2024. However, the 2024 limit remains $1,000.

**More SIMPLE IRA Contributions**



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SECURE 2.0 also brings new savings opportunities for small businesses with SIMPLE IRA plans. Beginning in 2024, higher salary deferrals and additional nonelective contributions will be allowed. And, starting in 2025, SIMPLE IRA participants aged 60-63 can make larger catch-up contributions.

**No Lifetime RMDs for Roth plans**

Do you have a Roth account in your employer plan? Here is a welcome change. Unlike Roth IRAs, Roth accounts in workplace plans have been subject to RMDs during the owner's lifetime. Beginning in 2024, this will no longer be the case – Roth plan dollars will be excluded from the RMD calculation.

**Expanded Exceptions to the 10% Early Distribution Penalty**

Generally, withdrawals from retirement accounts before age 59 ½ will be subject to a 10% early distribution penalty (in addition to the tax). However, there are a number of exceptions.

SECURE 2.0 added a slew of new 10% penalty exceptions for early withdrawals, with different effective dates. These include:

- Distributions for federally declared natural disasters - $22,000 limit (effective retroactively to 1/26/21)
- Terminal illness (effective 2023) – no limit
- 401(k) emergency savings accounts - $2,500 limit (effective 2024)
- Domestic abuse - $10,000 limit (effective 2024)
- Financial emergencies - $1,000 limit (effective 2024)
- Long-term care (LTC) - $2,500 limit (effective 2026).

In addition, the age 50 exception to the 10% early distribution penalty is extended to include public safety workers younger than age 50 with at least 25 years of service. Corrections officers and private sector firefighters are added to the list of public safety workers who can take advantage of this exception.



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***Early Withdrawal Caution:***
These new exceptions may be helpful if you need early access to your retirement funds. However, use these exceptions as a last resort. Distributions will most likely still be taxable, and every dollar taken early is a dollar you won't benefit from at retirement.

**Repayment of Qualified Birth or Adoption Distributions**
The SECURE Act allowed individuals to receive penalty-free distributions from their retirement account in the case of birth or adoption. There has been no time limit to repay these distributions. Now, there is a three-year repayment window.

**What's Not in SECURE 2.0?**
While there was talk of shutting down back-door Roth conversions and expanding QCDs to plans, neither of these items was included in the final legislation. Back-door Roth IRA conversions are still permitted, and QCDs are still limited to IRAs.

There was also discussion about limiting Roth conversions based on income, restricting certain IRA investments in start-ups and privately held stock, and forcing large RMDs when IRA balances of high-income individuals reached $10 million or more. These also did not get enacted, but they may be on the table for future legislation.

These proposals would upend existing planning strategies for retirement accounts, especially Roth IRAs. While these were not included in the SECURE 2.0 Act, they are still on Congress's radar.

**What's Ahead?**
The current Congress and administration may bring tax changes like these or others that could make future planning moves less attractive than they are now. We know the tax rules now and can plan with them, so it would be to your benefit to address your planning now while all current options, including low tax rates, are still available.

Based on all these new tax rules and factors in our lives, it is an ideal time to review and possibly revise our existing plans.

Even though the SECURE Act eliminated the stretch IRA for most non-spouse beneficiaries (grandchildren and adult children, for example), it has shined a light



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on options that may have been better strategies all along. The change in tax law now makes most larger traditional IRAs less desirable for estate planning purposes (i.e., less desirable to leave to beneficiaries), and Roth IRAs and cash value life insurance more desirable.

**Which IRAs are most affected by the elimination of the stretch IRA?**
The IRAs most impacted by the loss of the stretch IRA would be the larger IRA balances where a significant portion of your account will not be needed during your lifetime and will be passed on to your beneficiaries. The larger the portion left to your beneficiaries, the greater the tax impact will be for them, since most non-spouse beneficiaries will be forced to empty the accounts within 10 years after the death of the account owner.

**Impact on trusts.**
Many larger IRAs are left to trusts to exercise control over the funds your beneficiaries inherit. This is frequently done when you worry about beneficiaries who fall into these categories:

- Minors; the disabled; spendthrifts; those with creditor or financial problems; those facing lawsuits, bankruptcy, or messy divorces; those with family complications from second marriages; those with poor money management skills; and other beneficiaries who may be vulnerable and easily preyed upon.

**Trusts as IRA beneficiaries will no longer work well under the SECURE Act.**
After 10 years, someone must pay the taxes on the ***entire*** **taxable** IRA balance:
– Either the trust, at high trust tax rates (if the funds are held inside the trust to be protected), or

– By the individual trust beneficiaries at their own rates—but then the funds are no longer protected in trust.

If future taxes do increase, tax planning will be more critical than ever to preserve your retirement savings for yourself and for your beneficiaries. Updating your plans will take on new urgency.

Trusts as Roth IRA beneficiaries will work better since there will be no taxes when the funds go to the trust or to the trust beneficiaries.


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If you have named a trust as your IRA beneficiary, your plan needs an immediate review to make sure it complies with the SECURE Act, and it should probably be overhauled. Of course, this is something to review with your financial, legal, and tax advisors.

**Individual beneficiaries.**
Most IRAs are left directly to individual beneficiaries and not to a trust. However, the post-death payout term for most non-spouse beneficiaries (like a grandchild or adult child) will often be the same 10 years. The entire inherited IRA balance will have to be paid out to these beneficiaries at the end of the 10 years. And in some cases (when death occurs after RMDs had begun), beneficiaries also will be subject to RMDs for years 1-9 of the 10-year term.

## Conclusion: A replacement estate planning option is needed for IRAs and for other retirement accounts

**The three key objectives for a successful estate plan:**
Larger inheritances
More post-death control
Fewer taxes

**The SECURE Act problem:**
The SECURE Act could result in less post-death control and more taxes. Most people want the opposite result. One solution is permanent, cash value life insurance. This plan, which I call the **"Life Insurance Replacement Plan,"** will not only result in a more productive and less complicated estate plan, but it can also provide your family with the three key estate planning objectives outlined above.

## Life insurance as a solution:

**The SECURE Act makes permanent life insurance a more attractive estate planning vehicle than an IRA.**

**How the Life Insurance Replacement Plan works:**
You would begin by working with your financial and tax advisors to draw down IRA funds at the lowest possible tax cost. This can be done over several years,


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using up the lower tax brackets. While these distributions are taxable, they are being replaced with a more tax-efficient long-term estate plan, since they will be used to build tax-free funds inside a permanent life insurance policy.

**Caution: Avoid the 10% tax penalty**
There is a 10% early distribution penalty on IRA funds withdrawn before age 59½, so this strategy is not recommended for anyone under age 59½. Roth conversions may be a better option since they aren't subject to penalty, or you can wait until age 59½ when there will be no penalty.

Then use the retirement funds withdrawn (that were earmarked for beneficiaries) to purchase a permanent life insurance policy. If a trust is needed for post-death control, the life insurance can be owned by an insurance trust (an irrevocable life insurance trust, or ILIT).

**The sweet spot for planning—ages 59½ to 73.**
Take advantage of your "sweet spot." This is when you are between ages 59½ and age 73. During this period, IRA distributions are penalty free, but RMDs are not yet required. During this time, you have the most flexibility with your IRA, so it is an optimal time for taking IRA withdrawals for a Life Insurance Replacement Plan.

The sweetest spot of all for distribution planning may be between ages 59 ½ and 62. Distributions taken during this time period won't impact Medicare IRMAA charges for Parts B and D.

## Life insurance offers tax and estate planning advantages over IRAs —after the SECURE Act.

**Life insurance is more tax efficient.**
Life insurance will be income tax free to beneficiaries (except for the annual investment income).
Life insurance can also be estate tax free if it is set up outside the estate.

**Life insurance is more flexible when trusts are needed for post-death control.**
Life insurance is generally a better, more flexible, and more customizable asset to leave to a trust. It can simulate many aspects of the stretch IRA without the tax



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complications of an IRA trust. ***You can set the schedule and the terms of the trust*** by which you would like your beneficiaries to have access to the life insurance funds. There is no worry about who the trust beneficiaries or contingent beneficiaries are, or their ages, as there is with an IRA trust. Life insurance can be paid to an irrevocable life insurance trust (ILIT) so that the life insurance proceeds will be estate tax free. IRA funds can never be removed from the estate without being withdrawn.

A life insurance trust can be focused on ***your*** wishes, and you will not have to deal with the array of tax rules that you would have to work around with an IRA trust. It's simpler and more effective, with less tax intrusion. ***You get to focus on the plan you desire*** without worrying about tripping over the quagmire of IRA trust tax rules.

**Reliability.**
Life insurance can provide more certainty in a fast-changing world. As you have seen in just the last few years, both Congress and the IRS have historically changed tax laws frequently while leaving the treatment of insurance benefits alone.

**Leverage—life insurance provides leveraged wealth transfer.**
In most cases, more funds will go to the eventual beneficiaries, and with fewer taxes, than if the IRA was left directly to the beneficiaries or to an IRA trust subject to taxation. IRAs will be subject to the risk of potentially higher tax rates in the future. Generally, tax-free vehicles, like Roth IRAs and life insurance, avoid that risk.

## Lifetime benefits of —permanent insurance:

Life insurance can double as a tax-free retirement account.
– Life insurance can create additional tax-advantaged funds when other retirement plans are maxed out.
– Life insurance cash value can often be accessed in lieu of taxable retirement funds to keep taxes lower in retirement by creating a tax-free stream of income, if needed.

**Life insurance solves family money problems, without any of the tax restrictions that apply to IRA funds.**



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## Life insurance drawbacks:

Life is not perfect. Everything has a cost or downside, and you need to know both the pros and the cons before you make any financial decision. Life insurance is a long-term commitment, so doing a thorough evaluation and analysis is critical. Your family may be relying on this plan for decades. You should review all of the information that goes into this decision with your professional financial, tax, legal, and insurance advisors before taking any action.

This Life Insurance Replacement Plan as an alternative to the stretch IRA (which was largely eliminated by the SECURE Act) may not be for everyone. This strategy assumes that your IRA funds will not be needed during your lifetime, which is often the case for the larger IRAs. Other (non-IRA) funds will need to be available for lifetime use.

Not everyone is insurable. You must medically qualify for insurance coverage. No plan fits everyone, so this particular planning should be evaluated based on your personal financial situation and should be implemented only with professional guidance.

There is a current income tax expense when you use IRA money to fund the policy.

– This is about planning, however, for a better long-term tax benefit, and such long-term benefits often require a current investment. Tax rates are at a low point right now, and they could increase soon, possibly as early as 2026. If no action is taken now, your IRA funds will be forced out later through RMDs and may be more heavily taxed at that time if rates do rise. Using IRA funds now will reduce your IRA balance and, in turn, reduce your future income taxes by eliminating required minimum distributions on IRA funds.

**Life insurance is a long-term planning vehicle.**

– Policy premiums must be continually paid when due to keep the policy in force.

– It can take several years for substantial policy cash value to build up (but the death benefit is there from day one).



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Note: Lifetime policy withdrawals reduce the death benefit and available cash surrender value. Policy loans will also accrue interest at the current rate as well as reduce the death benefit and available cash surrender value.

## Planning steps

Considering the changes made by the SECURE Act, the recent IRS RMD rules and the SECURE 2.0 Act, it is essential that you review your current plan. Bear in mind that the new tax rules are already in effect. Begin by consulting with your professional advisors.

Evaluate the possible life insurance solutions described in this guide so you can meet the three most desired estate planning objectives:

- Larger inheritances
- More control
- Fewer taxes

Always consider both the benefits and the drawbacks of any financial, tax, or estate plan.

**Good advice is essential.**

The combined effects of SECURE Act, IRS RMD rules, the SECURE 2.0 Act and potentially new tax rules and tax rate increases have changed the tax, retirement and estate planning landscape for many. All these recent changes create uncertainty and raise doubts about the stability of your existing tax, retirement, and estate plans. You need more certainty and plans that can be relied on for the long term, and these recent tax rule changes could put the long-term stability of your plan at risk.

It's a good idea to review and update your current plans now in light of the current environment. Also, give some serious consideration to how the elimination of the stretch IRA for many beneficiaries will impact your family. Reconsidering your beneficiary designation for your IRA, converting traditional IRAs to Roth IRAs, and increasing the use of life insurance are all strategies that should be evaluated in the wake of the recent tax rule changes and your personal family health and financial situation.


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Do you have questions about your own situation? The SECURE Acts and other recent tax changes mean that now, more than ever, good advice is essential. A qualified financial advisor can help guide you through all the new rules and ensure that you are best positioned to take advantage of the breaks while avoiding the pitfalls.

—Ed Slott, CPA
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