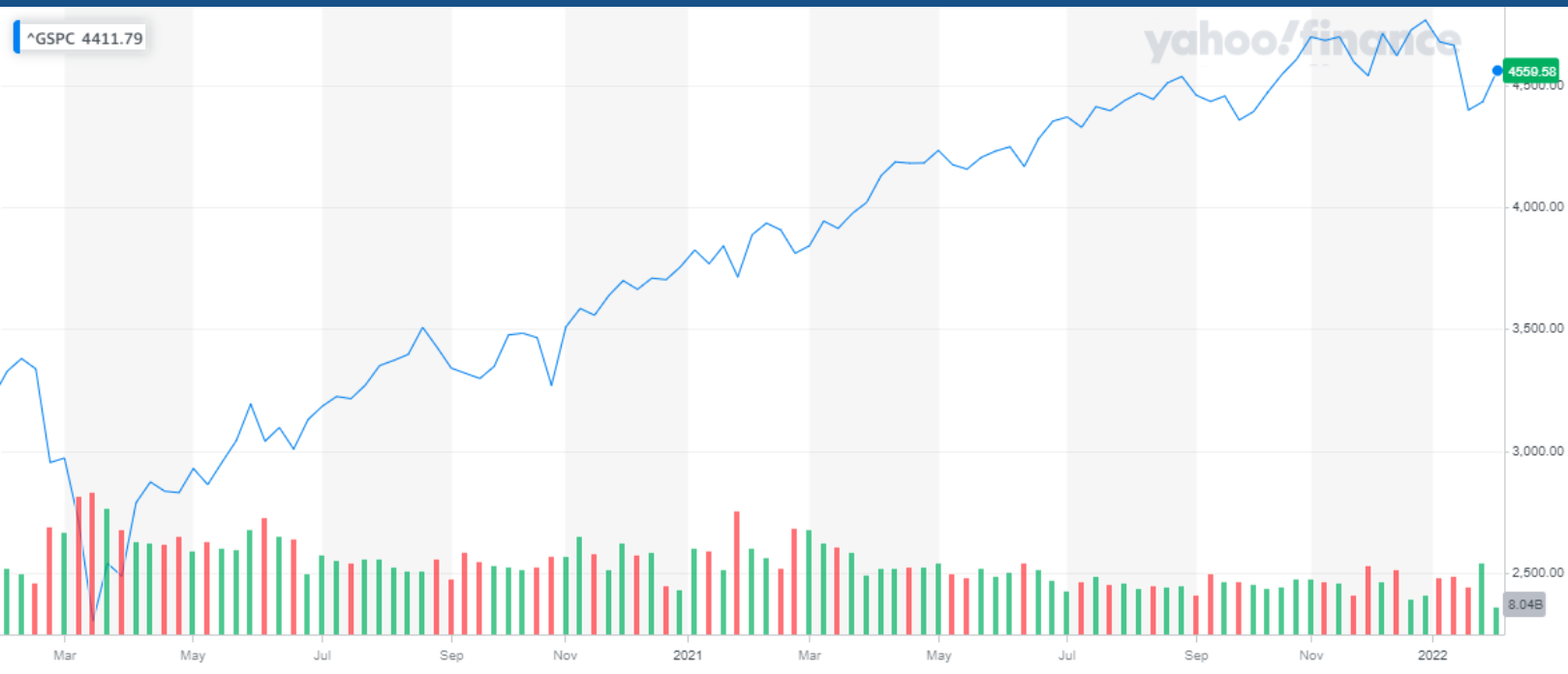




# Reexamining the SECURE Act



By: Michael L. Barsky, FSA, CFP®



**D**ecember 20, 2021 marked the 2<sup>nd</sup> anniversary since the passage of The Setting Every Community Up for Retirement Act of 2019, also known as the SECURE Act.

There have been dramatic changes in the U.S. during that two-year period:

- The COVID-19 epidemic continues to ravage the country, disrupting supply chains and driving up inflation
- The S&P500 Index shot up by over 41%<sup>1</sup>
- Over 6 million workers began receiving Social Security retiree benefits<sup>2</sup>

These sweeping societal shifts make it more important than ever to revisit the impact of the SECURE Act and consider alternative approaches for those intending to use their retirement account as part of their wealth transfer planning.

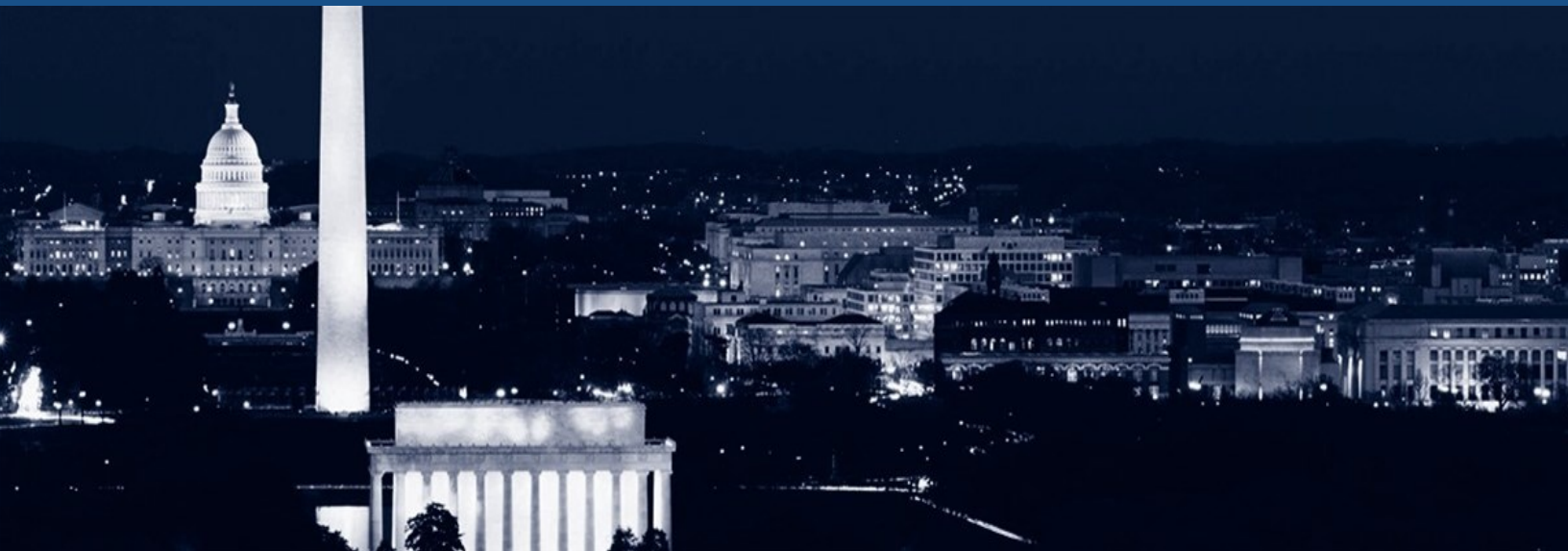
# Summary of Major Provisions of the Secure Act

This bill made several important, positive changes to retirement planning:

- Workers can now wait until age 72 before they must begin taking Required Minimum Distributions (RMDs) from their traditional Individual Retirement Accounts (IRAs) and employer tax deferred accounts such as 401(k)s, 403(b)s and 457s. Under previous law, the withdrawal requirement began at age 70 ½.
- Contributions to traditional IRAs are now allowed past age 70 ½, provided you have earned income.
- 401(k) plan administrators can now more easily offer annuities by shielding them from liability under a new safe harbor provision

However, to raise tax revenue to pay for the provisions of the Act, the rules regarding inherited retirement accounts were tightened for many non-spouse beneficiaries of account owners who died after December 31, 2019. Full distributions must now be made within 10 years as compared to previous law, where such beneficiaries were permitted to stretch out their required minimum distributions over the beneficiary's lifetimes. There are exceptions for beneficiaries with Special Needs, minor children, and beneficiaries less than 10 years younger than the original account owner.

These changes can have a significant impact on retirement account owners who have built up sufficient non-retirement assets, and now intend to use part or all of their accounts for transferring wealth. Since beneficiaries must now distribute all assets within 10 years, this can push them into a higher tax bracket.





## Case Study

John and his wife Susan are both 65 years and in good health, with two children Austin, 32 and Jessica, 28. John and Susan recently sold their business and are now fortunate to have accumulated sufficient assets (along with Social Security) to generate sufficient income to maintain their lifestyles in retirement, without relying on their retirement accounts.

John and Susan presently have \$2.5 million combined in their IRAs which they would like to pass on to Austin and Jessica. They have named each other as primary beneficiaries and their two children as equal contingent beneficiaries of their IRAs.

John and Susan live in Florida and are in the 32% federal tax bracket. They pay no state income taxes. Austin and his wife and two children live in Virginia and are at the high end of the 24% federal tax bracket, along with state income tax rate of 5.75%. Jessica is single and lives in New Jersey. She is in the 32% federal tax bracket and has a marginal state income tax rate of 6.37%.

John and Susan's retirement accounts are invested in a balanced portfolio which they expect will earn a 5% annual rate of return.

# Strategy #1

Under the new Secure Act rules, John and Susan can now postpone their RMDs until they reach age 72. At that time, they plan to begin taking RMDs and reinvest the net after-tax proceeds in a diversified account similar to the IRA, at an assumed 5% pretax return (3.4% after-tax)

- Following this plan, their combined IRA accounts will grow to \$3,517,751 by age 72
- The first RMD at age 72 will be for \$137,412 (equal to the prior year-end balance divided by the IRS Table III Uniform Lifetime rate of 25.6 at age 72)
- Assume that John dies at age 87. Susan inherits his IRA and continues to make RMDs
- Four years later, Susan dies at age 91
- At Susan's death, the remaining IRA balance is \$2,810,794.
  - Austin and Jessica each receive half this amount and must take full distributions within 10 years.
  - This extra income and career advancement pushes Austin into the 32% federal bracket. Jessica is still in the 32% federal bracket.
  - After federal and state taxes, Austin receives \$874,860 and Jessica is left with \$866,146
- In addition, the RMD Investment Account has grown to \$3,605,034 after taxes at Susan's death. This account is also evenly divided between Austin and Jessica.
- The IRA and RMD account will be part of John and Susan's taxable estate at Susan's death
- **The total net after-tax bequest to both siblings is \$5,346,040**

Age beg of year	IRA balance beg of year	RMD pretax	RMD After-Tax	RMD Investment Acct end of year	IRA Balance end of year	Age end of year
65	2,500,000	-	-	-	2,625,000	66
66	2,625,000	-	-	-	2,756,250	67
67	2,756,250	-	-	-	2,894,063	68
68	2,894,063	-	-	-	3,038,766	69
69	3,038,766	-	-	-	3,190,704	70
70	3,190,704	-	-	-	3,350,239	71
71	3,350,239	-	-	-	3,517,751	72
72	3,517,751	137,412	93,440	96,804	3,549,356	73
73	3,549,356	143,699	97,715	201,522	3,575,940	74
74	3,575,940	150,250	102,170	314,624	3,596,975	75
75	3,596,975	157,073	106,810	436,606	3,611,897	76
76	3,611,897	164,177	111,640	567,983	3,620,106	77
77	3,620,106	170,760	116,117	708,727	3,621,813	78
78	3,621,813	178,414	121,322	859,931	3,615,569	79
79	3,615,569	185,414	126,081	1,021,509	3,601,663	80
80	3,601,663	192,602	130,970	1,193,968	3,579,514	81
81	3,579,514	199,973	135,982	1,377,827	3,548,518	82
82	3,548,518	207,516	141,111	1,573,620	3,508,052	83
83	3,508,052	215,218	146,348	1,781,887	3,457,476	84
84	3,457,476	223,063	151,683	2,003,178	3,396,134	85
85	3,396,134	229,468	156,039	2,236,948	3,324,999	86
86	3,324,999	235,815	160,355	2,483,606	3,243,642	87
87	3,243,642	242,063	164,603	2,743,544	3,151,658	88
88	3,151,658	248,162	168,750	3,017,137	3,048,671	89
89	3,048,671	254,056	172,758	3,304,731	2,934,346	90
90	2,934,346	257,399	175,031	3,605,034	2,810,794	91

Hypothetical example for illustrative purposes only

#4097608.1 Expires 02/2024

# Strategy #2

Alternatively, John and Susan could reposition a portion of their IRAs by making combined annual tax-free gifts of \$64,000 to an Irrevocable Life Insurance Trust and purchasing a survivorship life insurance policy with a guaranteed death benefit of \$3,873,240. Austin and Jessica are each 50% beneficiaries. John and Susan immediately begin taking annual distributions of \$94,118 per year, of which 32% (\$30,118) goes to taxes and \$64,000 pays for the insurance.

- Following this strategy, using the same assumed dates of death as before, the remaining IRA balance at Susan’s death is \$2,167,876. Again, this amount is split evenly between Austin and Jessica, who must take full distributions within 10 years.
  - After federal and state taxes, Austin receives \$674,751 and Jessica is left with \$668,031
- The RMD Investment Account is \$1,015,836 after taxes. This account is evenly divided between Austin and Jessica
- Austin and Jessica each receive half of the \$3,873,240 of income and estate tax-free proceeds from the life insurance
- While the IRA and RMD account are still part of John and Susan’s taxable estate, the life insurance falls outside their estate and avoids double taxation.
- **The total combined net after-tax bequest to Austin and Jessica is \$6,231,858, which is \$885,818 more than the first strategy.**

Age beg of year	IRA balance beg of year	IRA Distribution for Life Ins pretax	IRA Distribution for Life Ins after tax	Additional Withdrawal for RMD pretax	Additional Withdrawal for RMD after tax	RMD Investment Acct end of year	IRA Balance end of year	Age end of year
65	2,500,000	94,118	64,000	-	-	-	2,526,176	66
66	2,526,176	94,118	64,000	-	-	-	2,553,662	67
67	2,553,662	94,118	64,000	-	-	-	2,582,521	68
68	2,582,521	94,118	64,000	-	-	-	2,612,824	69
69	2,612,824	94,118	64,000	-	-	-	2,644,642	70
70	2,644,642	94,118	64,000	-	-	-	2,678,050	71
71	2,678,050	94,118	64,000	-	-	-	2,713,129	72
72	2,713,129	94,118	64,000	11,864	8,067	8,358	2,737,505	73
73	2,737,505	94,118	64,000	16,713	11,365	20,432	2,758,008	74
74	2,758,008	94,118	64,000	21,765	14,800	36,501	2,774,232	75
75	2,774,232	94,118	64,000	27,028	18,379	56,856	2,785,741	76
76	2,785,741	94,118	64,000	32,507	22,105	81,803	2,792,072	77
77	2,792,072	94,118	64,000	37,584	25,557	111,225	2,793,389	78
78	2,793,389	94,118	64,000	43,488	29,572	145,865	2,788,573	79
79	2,788,573	94,118	64,000	48,886	33,243	185,556	2,777,848	80
80	2,777,848	94,118	64,000	54,430	37,013	230,581	2,760,765	81
81	2,760,765	94,118	64,000	60,115	40,878	281,232	2,736,858	82
82	2,736,858	94,118	64,000	65,933	44,834	337,804	2,705,649	83
83	2,705,649	94,118	64,000	71,873	48,874	400,598	2,666,641	84
84	2,666,641	94,118	64,000	77,924	52,988	469,915	2,619,330	85
85	2,619,330	94,118	64,000	82,864	56,348	545,208	2,564,465	86
86	2,564,465	94,118	64,000	87,759	59,676	626,661	2,501,718	87
87	2,501,718	94,118	64,000	92,578	62,953	714,439	2,430,773	88
88	2,430,773	94,118	64,000	97,282	66,152	808,692	2,351,343	89
89	2,351,343	94,118	64,000	101,828	69,243	909,541	2,263,167	90
90	2,263,167	94,118	64,000	104,406	70,996	1,015,836	2,167,876	91

Hypothetical example for illustrative purposes only

#4097608.1 Expires 02/2024

# Conclusion

Qualified retirement accounts continue to be an essential tool for accumulating and distributing assets to provide a secure retirement for millions of Americans. With the decline of traditional defined benefit pension plans and Social Security under strain, these retirement accounts will likely become an even more important piece in the retirement Income puzzle. However, the Secure Act changes in the distribution requirements for non-spouse beneficiaries make these accounts less efficient for passing on wealth to succeeding generations, particularly for families with estate tax exposure.

<sup>1</sup> Percentage change in S&P500 index between 12/20/2019-12/20/2021 [S&P 500 \(^GSPC\) Historical Data - Yahoo Finance](#)

<sup>2</sup> Social Security Administration - Number of new retired worker beneficiaries Jan 2020 – Nov 2021 [Beneficiary Data \(ssa.gov\)](#)

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Mike is our Director of Case Design and Client Services. He joined GWE in September 2021. Mike applies his extensive knowledge of life insurance to deliver clear and understandable presentations to assist clients as they make decisions regarding the structure and funding of new life insurance or optimizing the performance of their existing life insurance portfolios.

Greenberg, Wexler & Eig had the pleasure of working with Mike during his tenure as a Field Vice President for TIAA Life Insurance Company. Over the actuarial portion of his career, Mike was responsible for the design, pricing, and marketing of innovative insurance products at several of the country's largest life insurance companies, including John Hancock, Guardian Life and New York Life.

Mike is a Fellow of the Society of Actuaries (FSA) and a Certified Financial Planner (CFP®) and is one of the very few actuaries with firsthand experience as a financial representative. He is a graduate of Binghamton University and lives in Oyster Bay, NY with his wife, Lynne. They have two adult daughters; Danielle, a mechanical engineer and Sara, a registered dietitian.

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