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The SECURE Act: How Will It Impact Your Retirement Savings?

The Setting Every Community Up for Retirement Enhancement (SECURE) Act was recently passed into law. It will change several things that will affect your ability to save money for retirement and influence how you use the funds over time. Most of the changes are taxpayer-friendly measures designed to boost retirement savings. To get you up to speed, we've highlighted some of the most notable ways the SECURE Act impacts your retirement savings. Unless noted, all changes become effective January 1, 2020.

RMDS STARTING AT AGE 72

Required minimum distributions (RMDs) from 401(k) plans and traditional IRAs are a thorn in the side of many retirees. Right now, RMDs generally must begin in the year you turn 70½. (If you work past age 70½, RMDs from your current employer's 401(k) aren't required until after you leave your job, unless you own at least 5% of the company.)

The SECURE Act pushes the age that triggers RMDs from 70½ to 72, which means you can let your retirement funds grow an extra 1½ years before tapping into them. That can result in a significant boost to overall retirement savings for many seniors.

NO AGE RESTRICTIONS ON IRA CONTRIBUTIONS

Americans are working and living longer. So why not let them contribute to an IRA longer? That's the thinking behind the SECURE Act's repeal of the rule that prohibited contributions to a traditional IRA by taxpayers age 70½ and older. Now you can continue to put away money in a traditional IRA if you work into your 70s and beyond.

As before, there are no age-based restrictions on contributions to a Roth IRA.

401(K)S FOR PART-TIME EMPLOYEES

Part-time workers need to save for retirement, too. However, employees who haven't worked at least 1,000 hours during the year typically aren't allowed to participate in their employer's 401(k) plan.

That's about to change. Starting in 2021, the new retirement law guarantees 401(k) plan eligibility for employees who have worked at least 500 hours per year for at least three consecutive years. The part-timer must also be 21 years old by the end of the three-year period. The new rule doesn't apply to collectively bargained employees, though.

AUTO-ENROLLMENT 401(K) PLANS ENHANCED

More companies are automatically enrolling eligible employees into their 401(k) plans. Workers can always opt out of the plan if they choose, but most don't. Automatic enrollment boosts overall participation in employer-sponsored plans and encourages workers to start saving for retirement as soon as they are eligible.

The employer sets a default contribution rate for employees participating in an auto-enrollment 401(k) plan. The employee can, however, choose to contribute at a different rate. For a common type of plan known as a "qualified automatic contribution arrangement" (QACA), the employee's default contribution rate starts at 3% of his or her annual pay and gradually increases to 6% with each year that the employee stays in the plan. However, under current law, an employer cannot set a QACA contribution rate exceeding 10% for any year.

The SECURE Act pushes the 10% cap on QACA automatic contributions up to 15%, except for a worker's first year of participation. By delaying the increase until the second year of participation, lawmakers hope to avoid having large numbers of employees opt out of these 401(k) plans because their initial contribution rates are too high. Overall, the change allows companies offering QACAs to ultimately put more money into their workers' retirement accounts while keeping the potential shock of higher initial contribution rates in check.

HELP FOR SMALL BUSINESSES OFFERING RETIREMENT PLANS

It's simply harder to save for retirement if your employer doesn't offer a retirement savings plan, because all the work falls to you. Although most large employers have retirement plans for their workers, the same can't be said about small businesses. That's why the SECURE Act has three provisions designed to help more small businesses offer retirement plans for their employees.

First, the new law increases the tax credit available for 50% of a small business's retirement plan start-up costs. Before the SECURE Act, the credit was limited to $500 per year. However, the maximum credit amount is now up to $5,000.

Second, a brand new $500 tax credit is created for a small business's start-up costs for new 401(k) plans and SIMPLE IRA plans that include automatic enrollment. The credit is available for three years and is in addition to the existing credit described above. The credit is also available to small businesses that convert an existing retirement plan to an auto-enrollment plan.

Third, the SECURE Act makes it easier for small businesses to join together to provide retirement plans for their employees. Starting in 2021, the new law allows completely unrelated employers to participate in a multiple-employer plan and have a "pooled plan provider" administer it. This provision allows unrelated small businesses to leverage economies of scale not otherwise available to them, which typically results in lower administrative costs.

"STRETCH" IRAS ELIMINATED

Now for some bad news: The SECURE Act eliminates the current rules that allow non-spouse IRA beneficiaries to "stretch" required minimum distributions (RMDs) from an inherited account over their own lifetime (and potentially allow the funds to grow tax-free for decades). Instead, all funds from an inherited IRA generally must now be distributed to non-spouse beneficiaries within 10 years of the IRA owner's death. (The rule applies to inherited funds in a 401(k) account or other defined contribution plan, too.)

There are some exceptions to the general rule, though. Distributions over the life or life expectancy of a non-spouse beneficiary are allowed if the beneficiary is a minor, disabled, chronically ill or not more than 10 years younger than the deceased IRA owner. For minors, the exception only applies until the child reaches the age of majority. At that point, the 10-year rule kicks in.

If the beneficiary is the IRA owner's spouse, RMDs are still delayed until end of the year that the deceased IRA owner would have reached age 72 (age 70½ before the new retirement law).

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0052-MAM-2/4/20