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THE "YOU MAY NOT KNOW REPORT"

A PUBLICATION OF RETIREMENT LIFESTYLE ADVOCATES

SECURE Act Is Law. Is this an IRA and 401(k) Tax Grab?

Last year, here in the "You May Not Know Report", we told you about the SECURE Act, which had passed the House of Representatives by a wide margin and seemed to be stalled in the Senate.

It is stalled no more.

It is now law, effective January 1, with the President's signature last month.

The bill was included as part of a year-end spending package that contained eight bills and spending of $1.4 trillion[1], the SECURE Act is now law.

SECURE is an acronym for Setting Every Community Up for Retirement Enhancement. The act is considered to be the most sweeping retirement plan legislation since 2006 when the Pension Protection Act was passed.

In our view, while the SECURE Act does contain some beneficial provisions, it is also a tax grab and may require many IRA and 401(k) owners to rethink their estate plans and beneficiary designations. If you have an IRA or 401(k), you'll want to get up to speed as quickly as possible.

Let's dig in and look at the new law.The first change that the SECURE Act makes to IRA's and 401(k)'s is that the age at which required minimum distributions (RMD's) must begin has been raised from age 70 ½ to age 72.[2] This change is effective for those turning age 70 ½ after De-

cember 31, 2019.

If you are turning age 70 ½ January 1, 2020 or later, you may now wait until age 72 to begin taking your required minimum distributions. The "still working" required minimum distribution remains in place. If you don't own 5% or more of a company and continue to work past age 72, you can postpone distributions from that employer's retirement plan until the year after you retire.

The SECURE Act also changes the rules regarding IRA contributions. Now as long as you are working, you can contribute to a traditional IRA regardless of your age.[3] Previously, you could not contribute to a traditional IRA once you attained age 70 ½.

The SECURE Act also expands access to Multiple Employer Plans (MEP's). A MEP is a plan that allows employers to band together and pool resources to give employees access to retirement plans.

The SECURE Act also allows employers to auto-enroll employees in a plan at a savings rate of 6% of pay. Workers can opt out at any time.

The SECURE Act also allows plans to add annuities as investment options in employer sponsored retirement accounts. This is a big legislative victory for insurance companies which openly lobbied heavily for the bill.

529 plans were also revised under the SECURE Act. A 529 plan is a tax advantaged plan that allows for educational savings. 529 plan assets can now be used to pay for registered apprenticeships, homeschooling, up to $10,000 of qualified student loan repayments (including for siblings) and private elementary, secondary or religious schools.

The student loan provision allows for student loans to be repaid for a 529 plan beneficiary up to $10,000. An additional $10,000 can be used from the 529 plan to pay off student debt for each of the 529 plan beneficiary's siblings.

The SECURE Act would also allow investors to have early access to IRA funds for any 'qualified birth or adoption' without paying the 10% early withdrawal penalty. This change allows each parent to take a penalty-free withdrawal of up to $5,000. The withdrawal will be taxable but would not be subject to the 10% penalty.

But, as you undoubtedly gathered from the headline of this piece, the SECURE Act is not all good news in our view. The new law eliminates the stretch-out IRA that has been used as a cornerstone of estate planning for many IRA and 401(k) owners.

A non-spouse beneficiary (often a child) of an IRA or 401(k) had the ability to inherit the retirement plan and spread the taxes on the inherited account over his or her lifetime prior to the passage of the SECURE Act. For example's sake, a 50-year-old child inheriting an IRA from a parent could take minimum distributions based

on his or her life expectancy, pay tax on the distribution but allow the remaining IRA balance to continue to grow on a tax-deferred basis.

According to the IRS' life expectancy table, a 50-year-old has a life expectancy of another 34.2 years. That means that prior to the SECURE Act becoming law, that 50-year-old would have to take the inherited retirement account balance at the end of the year and divide that total by 34.2 to determine the required distribution from the inherited IRA.

The next year, the IRA beneficiary would adjust the divisor by subtracting 1 from it. In this example, the 34.2 would be adjusted to 33.2 (34.2 – 1 = 33.2). The prior year end balance would be divided by 33.2 to get the new required distribution for the current year.

In this way, should the beneficiary elect, the inherited IRA could be maintained for their life expectancy. In this example, to age 84.

That stretch out option is no longer available under the new law.

The SECURE Act mandates that inherited IRA's, 401(k)'s and Roth IRA's be totally distributed within 10 years of inheriting them.

This creates several possible problems as outlined in a recent "MarketWatch" article[4] (emphasis added):

> *But under the SECURE Act,* ***there are no required minimum distributions for inherited IRAs*** *(known as the "stretch IRA").* ***With the new law, beneficiaries need only ensure all of the money is taken out within 10 years. These rules also apply to inherited 401(k) accounts, regardless of whether they are rolled into IRAs, as well as Roth IRAs.***
>
> ***The only technical required minimum distribution is after the 10th year, which would be the remaining balance.*** *In the case of an inherited IRA through a trust, that would be the entire amount, with no opportunity to take out money during the 10-year wait.*
>
> *There are no tax breaks for taking funds from traditional IRAs, and the same applies to inherited IRAs. That means payments will be taxed at the beneficiary's income tax bracket, said John Iammarino, principal and founder of Securus Financial.* ***The drain-in-10 rule can result in a large tax bill for a beneficiary, especially if that person is in their 40s or 50s, which is typically the peak earning years.***
>
> *"If you do have an IRA trust, get it reevaluated to make sure the language in it is not going to do anything to be detrimental," Iammarino said.*
>
> *The elimination of the stretch IRA alone has the potential to generate about $15.7 billion in tax revenue over the next decade, according to* the *Congressional Research Service*. ***The SECURE Act as a whole is expected to generate $16.4 billion over the next 10 years.*** *Other provisions of the law include allowing employers to more freely offer annuities as options in a 401(k) and expanding access to retirement plans* for small business workers.

The article is referring to the fact that many IRA owners utilized an IRA Inheritance Trust as part of their estate plan. Or, their trust stipulates that their child, when inheriting their IRA or 401(k) must take the distributions rather than the lump sum. This was done to prevent a child who was inheriting a lot of money in a retirement account from blowing through the money.

These trusts or trust provisions may now put the beneficiary in danger of not being able to access the inherited IRA funds for 10 years and then require a one-time, completely taxable

distribution.

If you have an IRA and a written estate plan, you may want to make a review of your IRA beneficiaries and your estate plan a high priority New Year's Resolution.

The SECURE Act makes leaving an heir money in a retirement account far less desirable.

And, it makes Roth conversions that much more attractive for some IRA owners, especially those who plan to pass most of their retirement savings on to a non-spouse beneficiary.

We have advocated that these types of clients consider Roth conversions given the lower income tax rates in effect until 2026. Now, with the advent of the SECURE Act, it makes even more sense. A recent "Forbes" piece does a nice job of explaining this strategy[5] (emphasis added):

> *Given that IRAs will now have to be distributed within ten years, generally, the beneficiary will pay taxes at a higher rate. Even spreading the distribution equally over those ten years will result in much higher taxes in most cases.* ***Consider the example of a 25-year-old granddaughter receiving a $1 million IRA from her grandmother, the additional tax created by the accelerated distribution amounted to around $400,000****. Roth IRAs are subject to the 10-year rule, but Roth's are distributed tax-free.* ***The 10-year rule allows beneficiaries of Roth IRAs to continue the tax-free growth for 10-years.*** *This growth opportunity now opens some analysis of intergenerational Roth strategies, including what I call the 'Mom Roth.'*
>
> *The best way to illustrate the Mom Roth is what I did for my own mother. My mother was a depression-era baby (born in 1921). She was thrifty and a good saver, even though my Dad was a machinist and my Mom a bartender. Dad built up a modest 401(k) and left it to my mom when he passed. When she was 70 ½, she started taking Required Minimum Distributions, which irked her. I prepared her taxes and noticed she had ample room in her low tax bracket for additional income. Mom's tax rate was well below that of my sister or me. We converted enough to 'bracket-top' her to the top of her bracket.*
>
> *A single, older person could have $52,975 of income and pay only $4,543 in taxes. Converting to Roth at those rates can be very beneficial. We used other funds to pay the taxes on the conversion.*

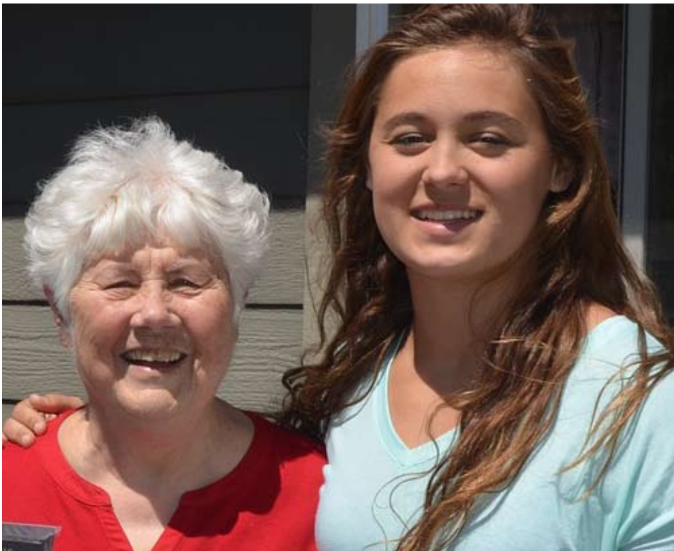
As usually happens, the changes brought on by the SECURE Act may create opportunity for many IRA and 401(k) plan owners.

One way to potentially establish a stretch-out like outcome under the new rules would be to establish a Charitable Remainder Trust that would be the beneficiary of the IRA or 401(k) account. The income beneficiary of the Charitable Remainder Trust would be the IRA beneficiary, typically a child.

Since distributions from a Charitable Remainder Trust are calculated based on the life expectancy of the beneficiary, the equivalent of a stretch out may be able to be established. This strategy could be combined with a life insurance trust to replace the portion of the IRA going to charity.

Here is a hypothetical example to make the possible outcome more clear:

A 72-year-old female has $1,000,000 in her IRA. She plans on taking only required minimum distributions and leaving her IRA balance to her only daughter at her death. Her daughter is presently 47 years old.



Currently, her required minimum distribution will be just under $40,000 and then increases from this point on. Assuming a 5% growth rate and taking only required minimum distributions, at her death (assuming death at age 90), her IRA balance will be about $834,000. Under the new law, her daughter will have to distribute and pay taxes on the entire IRA balance within 10 years. (Note: If returns other than 5% are realized, the outcome illustrated here could be significantly different.)

What if this 72-year old client decided to establish a charitable remainder trust and name her daughter the income beneficiary?

The daughter, in this hypothetical example would be 65 years of age. Assuming the charitable remainder trust was established with a 5% payout to the daughter and the assets continued to earn 5% annually, the daughter would receive income of $41,700 annually for as long as she lived. At her passing, a charity would receive the $834,000 in the trust.

There is no tax on the IRA transfer to the charitable trust on the death of the original IRA owner and no tax on the ultimate distribution to charity. Only the distributions to the daughter of $41,700 per year would be taxable.

The original 72-year old client could opt to combine this strategy with a life insurance trust in which she purchases a life insurance policy on her life in the amount of $1,000,000. The annual premium is $25,000. She pays this using her IRA assets. This strategy will reduce the ultimate benefit to charity but increase the net benefit to her daughter.

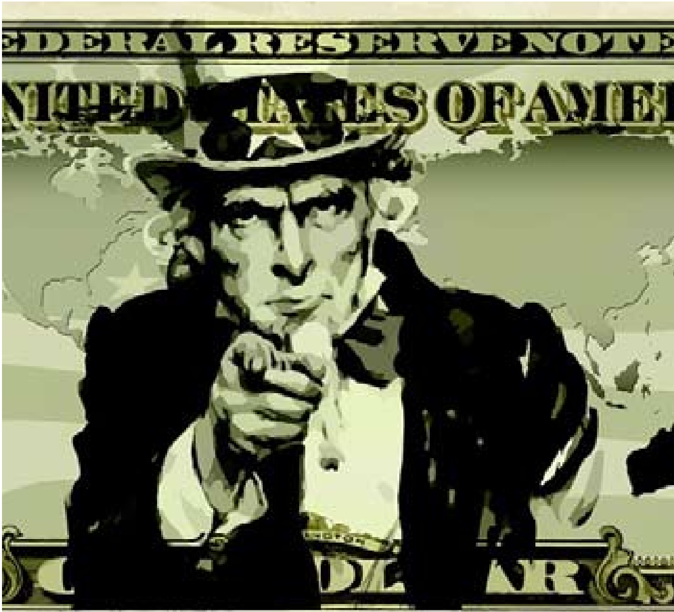
Let's compare outcomes:

No CRT, RMDs Only	
Income withdrawn	$ 1,078,113
Total Taxes (assuming a 25% tax rate for client and daughter)	$ 478,067
Net Benefit	$ 625,616
Net to Charity	$ 0

CRT, RMDs + Premium Net of Tax	
Income withdrawn	$ 1,078,113
Additional withdrawals for Premium (gross)	$ 600,000
Total Taxes (assuming a 25% tax rate for client and daughter)	$ 332,828
Net Benefit	$ 1,281,788
Net to Charity	$ 300,574

Nice outcome isn't it? Client takes the same income. Daughter gets a net benefit of nearly double. And a charity wins that wouldn't have otherwise received anything. It's important to note that the IRA balance at the client's death is lower using the CRT because the IRA is funding life insurance premiums.

If you're likely leaving retirement account assets to children, you might want to take a look at this Salvage Your Stretch™ strategy.



It's the Debt Stupid

Many of you who are old enough undoubtedly remember the Clinton campaign rallying cry – "it's the economy stupid".

While today's economy is good by all outward measures including the unemployment rate which is undeniably good, there is a looming issue that not one politician has yet chosen to address, at least as far as we've seen. And, that problem is the out-of-control Federal spending and debt accumulation.

While there are those who would like to have us believe that one party is more to blame than another for this problem, the numbers tell us otherwise. Ever since the link between the US Dollar and gold was eliminated, the debt monster has simply grown.

Here is a look at the size of the official national debt by President based on the end of the fiscal year (September 30): [6]

President	FY End	Debt (Billions)	Increase %
Nixon	1974	$ 475	
Ford	1976	$ 600	26.3%
Carter	1980	$ 908	51.3%
Reagan	1988	$ 2,602	186.6%
Bush	1992	$ 4,065	56.2%
Clinton	2000	$ 5,674	39.5%
Bush (W)	2008	$ 10,025	76.7%
Obama	2016	$ 19,573	95.2%
Trump	2019	$ 22,776	16.36%

The point is this.

This cannot continue. History teaches us it will end and with the end will come ugly economic and financial consequences.

Past radio guest, John Mauldin, wrote a piece[7] on this recently titled "A Crisis Has Already Begun". Here is an excerpt (emphasis via red font added):

The US government ran a $343 billion deficit in the first two months of fiscal 2020 (October and November), and the 12-month budget deficit again surpassed $1 trillion. Federal spending rose 7% from a year earlier while tax receipts grew only 3%.

No problem, some say, we owe it to ourselves, and anyway people will always buy Uncle Sam's debt. That is unfortunately not true.

The foreign buyers on whom we have long depended are turning away, as Peter Boockvar noted:

Foreign selling of US notes and bonds continued in October by a net $16.7b. This brings the year-to-date selling to $99b with much driven by liquidations from the Chinese and Japanese. It was back in 2011 and 2012 when in each year foreigners bought over $400b worth. ***Thus, it is domestically where we are now financing***

our ever-increasing budget deficits.

The Fed now has also become a big part of the monetization process via its purchases of T-bills which also drives banks into buying notes. The Fed's balance sheet is now $335b higher than it was in September at $4.095 trillion. *Again, however the Fed wants to define what it's doing, **market participants view this as QE4 with all the asset price inflation that comes along with QE programs**.*

It will be real interesting to see what happens in 2020 to the repo market when the Fed tries to end its injections and how markets respond when its balance sheet stops increasing in size. It's so easy to get involved and so difficult to leave.

Declining foreign purchases are, in part, a consequence of the trade war.

The dollars China and Japan use to buy our T-bills are the same dollars we pay them for our imported goods. But interest and exchange rates also matter. With rates negative or lower than ours in most of the developed world, the US had been the best parking place.

*But in the last year, other central banks started looking for a NIRP exit. **Higher rate expectations elsewhere combined with stable or falling US rates give foreign buyers—who must also pay for currency hedges—less incentive to buy US debt.***

If you live in a foreign country and have a particular need for its local currency, an extra 1% in yield isn't worth the risk of losing even more in the exchange rate.

I know some think China or other countries are opting out of the US Treasury market for political reasons, but it's simply business. The math just doesn't work.

Especially when President Trump is explicitly saying he wants the dollar to weaken and interest rates go even lower.

If you are in country X, why would you do that trade? You might if you're in a country like Argentina or Venezuela where the currency is toast anyway. But Europe? Japan? China? The rest of the developed world? It's a coin toss.

The Fed began cutting rates in July. Funding pressures emerged weeks later. Coincidence? I suspect not.

It sure looks like, through QE4 and other activities, the Fed is taking the first steps toward monetizing our debt. If so, many more steps are ahead because the debt is only going to get worse.

We'd encourage you to follow the link below to read Mr. Mauldin's entire piece.

In the excerpt reproduced here, there are several important points that should not go unnoticed by you. Nor should you delay taking action on these developing trends if you have not already done so.

Mr. Mauldin notes that the debt is only going to get worse.

We'd have to agree based on the debt table we assembled at the beginning of this piece. While some Presidents were better than others when it came to debt accumulation. There was not one President who managed to keep from feeding the debt monster.

At this point, we need to digress for a moment to make an interesting point.

When taking a look at the level of national debt at the end of President Nixon's time in office and comparing it to the national debt at the end of fiscal year 2019, the debt increased by almost 48-fold.

Long time readers of this publication are aware that is was President Nixon who took the nation off the semi-gold exchange standard in 1971. At that time, the price of gold per ounce was $35; today gold is back to more than $1500 per ounce. That's an increase of almost 45-fold.

In other words, reserving the national debt in gold in 1974 would almost pay the national debt today. Should anyone try to dissuade you from having some gold in your portfolio, remember this simple fact.

If the debt is only going to get worse as Mauldin states and as we would all likely agree, and the reasons that existed for foreign entities to buy US debt have disappeared, the only other option as Mauldin states is to deal with the deficit domestically.

There are only three ways to do that.

One, cut spending. One needs only to visit the websites of any of the politicians aspiring to the position of commander-in-chief to quickly realize this option is not on the table.

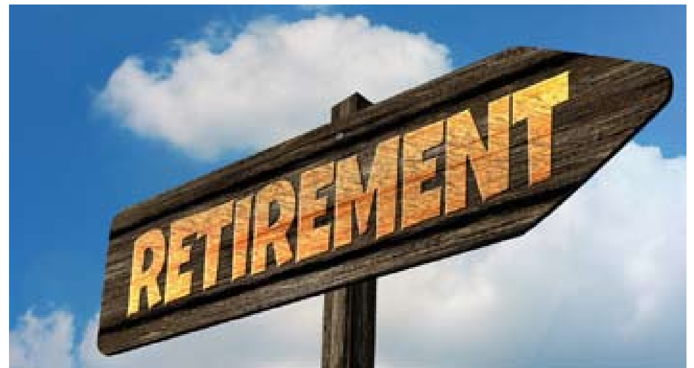
Two, raise taxes. Don't shoot the messenger, but the debt on unfunded liabilities cannot be paid and funded through taxes; there is simply not enough money in existence. Confiscating 100% of household wealth will not pay off the national debt and fully cover the unfunded liabilities of Social Security and Medicare.

Three, as Mauldin states – monetize the debt and the deficits.

Monetize is a verb that means to create money.

Foreigners recognize this and are dumping US Dollar denominated assets. As Mauldin notes, this year there has been net selling of US Treasuries of $99 billion while just 7 years ago, there was net buying of more than $400 billion.

The money creation is sure to continue in our view. Moving to more tangible assets in one's portfolio is something many investors should consider.



The New Normal When It Comes to Retirement?

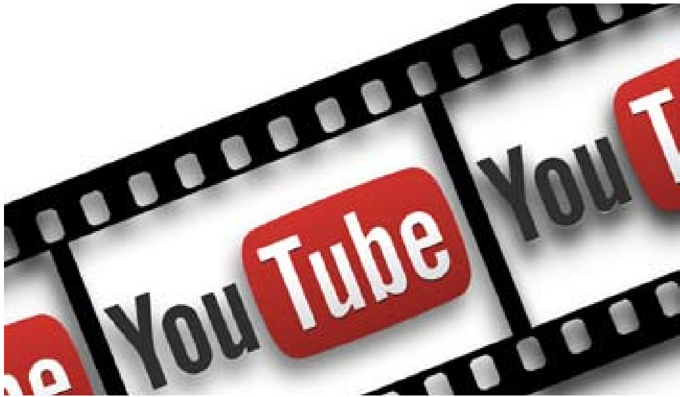
According to an MSNBC article[7], the majority of American workers now say they plan to retire after age 65 or never retire.

Transamerica Center for Retirement Studies did a survey on which MSNBC reported. Among the survey's findings:

- 14% of American workers have no plans to retire
- 40% of American workers plan to retire after age 65
- 24% say they will retire at age 65
- Only 22% say they will retire prior to reaching age 65.

The primary reason people keep working is that they haven't yet saved enough money to retire. But, running a close second is their concern for healthy aging. Many who were surveyed were concerned about staying active and didn't want to be isolated socially.

Three in four workers surveyed were concerned that Social Security would not be there for them when they decided to retire.



8-Year Old Earns $26 Million on YouTube

Ryan Kaji, an otherwise normal 8-year old boy, pocketed a cool $26 million last year reviewing toys on You Tube.[8] That's according to "Forbes".

Ryan's You Tube channel is called "Ryan's World" and it has more than 22 million subscribers. Ryan simply opens the boxes containing the toys on camera, then unpacks the toy and comments on it.

While Ryan was number one in earnings, another child, five-year old Anastasia Radzinskaya, came in third place with earnings of $18 million last year.

Radzinskaya, who was born in southern Russia and has cerebral palsy, appears in videos with her father. According to Forbes, she has 107 million subscribers across seven channels and her videos have been watched 42 billion times.

One of her most successful videos was filmed on a trip to a petting zoo, where her and her dad danced to "Baby Shark."

Dude Perfect – a group of five friends in their thirties who play sports and perform stunts – came in second place, earning $20 million.

YouTube has announced that next year it will stop personalized advertisements on children's content.

This comes after Google agreed to pay $170 million to settle accusations that YouTube broke the law when it knowingly tracked and sold ads targeted to children.

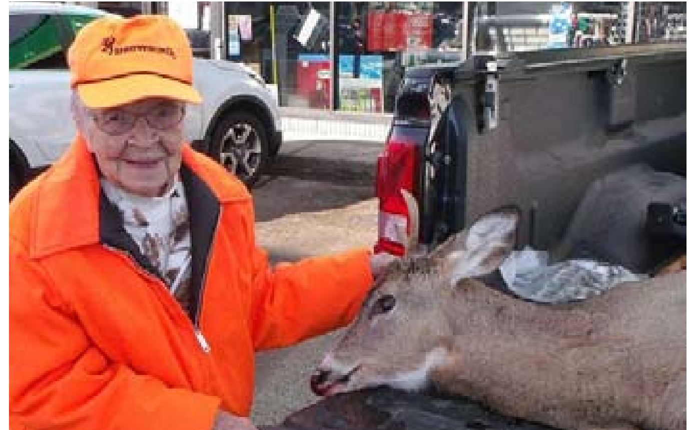


Photo: Wisconsin Department of Natural Resources

104-Year-Old Hunter Harvests Deer

Let's hear it for Florence Teeters.

The 104-year old Wisconsin native became the state's oldest hunter to harvest a deer this past season. This from WCCO:[9]

> *A 104-year-old woman has bagged a buck to become the oldest person in Wisconsin to ever harvest a deer.*
>
> *The Department of Natural Resources says Florence Teeters was inspired to purchase her first hunting license while sitting in a blind on her land in Price County with her son, Bill, during last year's gun deer season.*
>
> *She and Bill set up their blind on Saturday, opening day of the 2019 nine-day gun season. Two hours into their day they saw a spike buck and Florence took it down. Bill says she was excited and kept saying "I got a buck! I got a buck!"*
>
> *DNR officials say a preliminary check of records indicates Florence is the oldest person to date to purchase a gun deer license and harvest a deer.*

Auto Industry – Subprime Woes Coming?

According to a recent "Zero Hedge" article[10], the auto industry has verified income on just 7% of loans since 2017. What could go wrong?

This from the article (emphasis added):

> ***The auto industry in 2019 is starting to look a lot like the subprime mortgage market in 2007.***
>
> *One such example of an industry trying to move vehicle inventory by any means necessary was Mirna Lopez, a 65-year-old who was able to buy a 2018 Nissan Pathfinder on monthly earnings of just $660. Her car loan's monthly payment was slated to be $809.*
>
> *How was this possible? The Wall Street* Journal reports *that an employee at the dealership that sold her the car simply listed her monthly earnings at $7,833. Nothing creative, nothing fancy: just plain old fraud.*
>
> *It's no longer good enough for customers to be buying cars with debt only. Now, while the auto industry struggles to pull itself out of the recession it is mired in, some dealerships around the country are "dressing up" loan applications with fake incomes, according to consumer lawyers.* ***Additionally, some large lenders have cut back on safeguards that could catch the fraudulent applications****.*
>
> *The result is usually a quick default on these loans and consumers destroying their credit.*
>
> *Richard Feferman, a New Mexico lawyer who has sued dealerships and lenders said: "The consequence for a lot of people is to ruin them financially for five to 10 years."*
>
> *The amount of false applications is "hard to quantify" according to PointPredictive, which sells software to detect loan fraud.* ***The company estimates that more than 20% of loans have inflated incomes.***
>
> *Of course,* ***dealers have the option to ask for documentation to prove income, but over the past few years some subprime lenders have stopped checking them - partly in response to dealers demanding faster decisions. In fact, lenders verified income on only about 7% of all loans since 2017, the Journal found.***

Defaults to follow.

Do You Know How You Will Be Affected by the SECURE Act?

The SECURE Act is now law. Your IRA or 401(k) will be affected as the rules have changed.

While some parts of the SECURE Act can benefit some taxpayers, there are other parts of the new law that will require taxes be paid more quickly. And, there are opportunities for many IRA and 401(k) investors to actually divorce themselves from the IRS in their IRA and 401(k). Don't miss out on your opportunity to save money on taxes.

The details of this just-passed, new law will be revealed at a free, informational meeting to be held at Sunnybrook Country Club in Grandville on January 28. The meeting will begin at 6:00 PM and conclude at 7:30 PM with a complimentary dinner. Tickets to the event are free but required. (Please limit your ticket requests to no more than 4 tickets.)

If you have an IRA or 401(k) and will be eligible to collect Social Security during retirement, <u>you should attend</u>.

This free meeting will show you:

- How to potentially, **significantly reduce taxes on your IRA or 401(k) plan**
- How, under the law, planning strategies **exist that may allow you to pay zero taxes during retirement.** These planning strategies are potentially favorable for only a **limited time**
- Why maximizing Social Security benefits will not work **unless you address the ultimate tax liability on your retirement account**
- Why the tax deduction you get for contributing to an IRA or 401(k) can be a bad thing. **This tax deduction may ultimately end up costing you more than you benefit.**

Tickets for the event are required but available by visiting <u>www.TaxFreeInRetirement.com</u>.

Or, you may call 1-866-879-0137 ext. 1207 anytime, 24 hours per day, 7 days per week with your ticket requests.

IMPORTANT! There will be <u>no presentation to buy financial products</u> at this meeting. The meeting is <u>informational only</u> in nature.

Communication Note Reminder

To provide you with the best possible service and best response time, please remember to call the office rather than communicating via e-mail. Just let the receptionist know what we can do to help, and you'll be put in touch with the right person or have a call scheduled with you and the right person at a mutually convenient time.

The office phone number is:

1-866-921-3613

Our office hours:

Monday to Thursday, 8:00 AM to 5:00 PM

Fridays from 8:00 AM until Noon.

Sources

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