YOUR MONEY

AX REPORT

Planning to Leave an IRA to the Grandkids? Not So Fast.

Congress aims to curtail Stretch IRAs, which pass on decades of tax-free growth to young heirs; 'the government is breaking its promise to me.'

Joseph Folk with three of his grandchildren in Norfolk, Va., in 2016. **PHOTO:** JOSEPH FOLK

By Laura Saunders

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Joseph Folk feels betrayed.

Mr. Folk, a 72-year-old retired middle manager for railroads living in Norfolk, Va., is a rigorous saver. He says his two cars are 14 and 24 years old—"and they run fine"—and he hasn't bought any new clothes in years.

A decade ago, after providing for his wife and two children, Mr. Folk decided to extend the life of his savings by arranging for his four grandchildren to inherit individual retirement accounts, or IRAs, each worth more than $1 million.

Mr. Folk made this move because when young people inherit either a traditional IRA or a Roth IRA, the accounts can benefit from decades of tax-free compounding after the original IRA owner dies. That's why they're called Stretch IRAs.

Mr. Folk says he paid well over $1 million of tax to carry out his plans by converting the accounts for his grandchildren, ages 10 to 14, from traditional IRAs to Roth IRAs. That way, he wouldn't have to take withdrawals while alive, and his grandchildren's required payouts could be tax-free.

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Now Congress may throw a wrench in Mr. Folk's planning. The House of Representatives has passed a bill reducing Stretch IRAs to a maximum of 10 years for heirs like Mr. Folk's grandchildren.

Critics of Stretch IRAs for younger heirs say they are a boon primarily for the wealthy, who can afford to forgo spending their retirement savings during life. The critics say the tax dollars are better used for other savings incentives, and they have strong support.

In May, the House passed its version of the changes in the SECURE Act by 417 to 3. Kevin Brady, a Texas Republican who chaired the House Ways & Means Committee through 2017, favors the legislation.

"IRAs are for retirement security. They are not wealth succession management tools, and I think we've now got the policy right," Rep. Brady said in late August.

The Senate is considering both the House's bill and one of its own. For Mr. Folk and others who have made such plans, the proposed changes are a shock.

"All my life I've carefully saved for my family and grandchildren. Now the government is breaking its promise to me. They should only change the rules going forward, not retroactively," he says.

The current rules, in effect since 2003, typically allow required annual withdrawals to be taken over an heir's expected lifespan. For example, a 23-year-old who inherits an IRA can take required payouts over 60 years while the assets keep growing.

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Mr. Folk's predicament illustrates one peril of long-term financial plans. Congress has a right to change tax laws and does. In the words of a 1938 court opinion, "Every deduction . . . is allowed as a matter of legislative grace."

Ed Slott, a Certified Public Accountant in Rockville Centre, N.Y., who is an IRA specialist, estimates that with the current-law stretch of 60 years, a 23-year-old heir of a $1 million Roth IRA could receive a total of $23 million.

But with a 10-year stretch, the heir could receive a total of $16 million, about 30% less. Mr. Slott's estimates assume a 6% annual rate of return, a 25% average tax rate where applicable, and no withdrawals from the Roth IRA under the new rules until the end of the 10th year. Amounts are unadjusted for inflation.

Opponents of the proposed changes say they set a dangerous precedent.

"This is not a fair way to conduct retirement policy, changing the rules near the end of a long game. People will think they can't trust Congress to keep its word about retirement rules," says Mr. Slott.

There are similarities and differences in the House and Senate proposals. Both allow the stretch for a large number of "eligible" heirs. These include surviving spouses, disabled or chronically ill heirs, an heir close in age to the IRA owner such as a sibling, and minor children of the IRA owner.

The House's SECURE Act puts a 10-year limit on the stretch provision for "non-eligible" heirs such as grandchildren or children who aren't minors. There would be no required annual withdrawals from inherited IRAs during the 10-year term, only at the end. The proposed changes would take effect for IRA owners who die after Dec. 31, 2019.

The Senate's bill, which hasn't passed, allows the "non-eligible" heirs like grandchildren to use the current stretch rules if their inherited IRA is $400,000 or less. Otherwise, the IRA assets for these heirs must be withdrawn within five years.

Current data on inherited IRAs isn't available. The House's version of the Stretch IRA restrictions is estimated to raise $15.7 billion from 2019-2029. There's not a revenue estimate for the Senate bill, and it's unclear when the Senate will act.

Until there's clarity, people hoping to leave Stretch IRAs to younger heirs will likely pause their planning.

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