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OPINION | REVIEW & OUTLOOK

IRAs in Political Sights

Forcing some heirs to empty accounts in 10 years will raise revenue, but it's a bad precedent.

By The Editorial Board
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Putting money into a 401(k) or Individual Retirement Account is an act of trust in government. When yesterday's politicians set rules to encourage saving, workers must have faith that tomorrow's politicians won't raid the kitty. Protecting this confidence ought to be top of mind as the Senate takes up the bipartisan Secure Act, which sailed through the House this summer 417-3.

The bill is a 125-page mashup of mostly uncontroversial updates to the nation's retirement rules. Today contributions to a traditional IRA can't be made past age 70½, which is also when mandatory distributions kick in. Lifespans and careers now are stretching longer, so the Secure Act sensibly eliminates the contribution age limit while allowing distributions to be delayed until 72.

Early withdrawals are often subject to a 10% tax penalty, with a few exceptions. The Secure Act would add a new one, allowing $5,000 to be taken out when a child is born or adopted. Another provision would require company 401(k) plans to cover part-time employees who work at least 500 hours for three years running.

Donald Trump vs. the Democratic House 'Squad.'

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The hangup is that broadening such tax advantages will cost the government money. The Secure Act pays for itself, though only by suddenly curtailing tax benefits on retirement assets passed down to children, grandchildren and other non-spousal heirs. New rules would apply to account holders who die starting in 2020. For people with significant money, this could upend years of careful estate planning.

Under current law, a 5-year-old grandson who inherits money in an IRA can "stretch" the mandatory distributions over his lifetime. That allows for longer tax-free growth, giving legacy-minded investors a way to build family wealth. The Secure Act would require the IRA to be emptied within 10 years. This would speed up the tax liability, which could also push the bunched-up distributions into a higher tax bracket.

Maybe there's an argument that IRAs weren't meant to be used as vehicles for inheritance. Nevertheless they are, and the figures can be large. Mitt Romney's retirement account made news in 2012 when financial disclosures, which specify wealth in ranges, said his IRA held between $21 million and $102 million. Those numbers were thought unusual, a result of savvy investments Mr. Romney made in Bain Capital projects.

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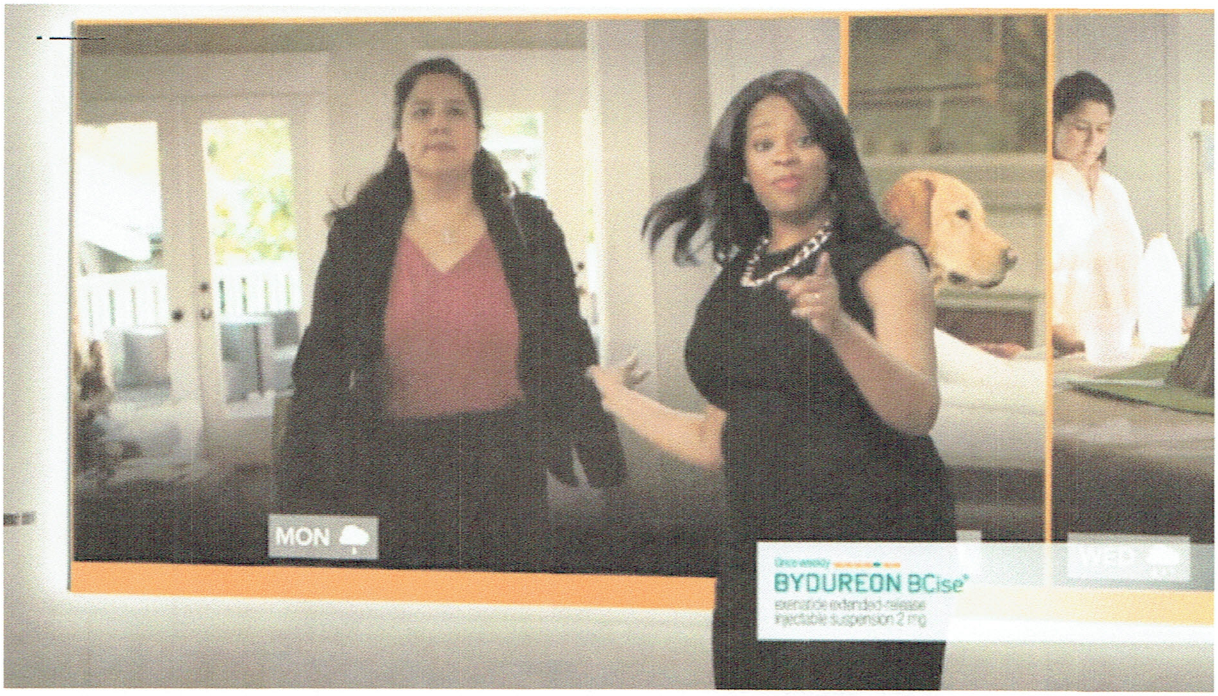
Still, you may be surprised: Fidelity Investments says that its last census of 401(k) millionaires includes 180,000 of its account holders, along with 168,000 IRA millionaires, plus another 22,000 educational workers or nonprofit staff who are 403(b) millionaires. And that's only Fidelity. Some 33,000 federal workers have accumulated $1 million or more in their Thrift Savings Plan accounts, which can be rolled into IRAs.

Rather than spend this on wine and cruises, some of these people may prefer to pass on as much money as possible, perhaps to help their grandchildren pay for college or starter houses. If savers spent years building up their accounts with that goal in mind, it is hardly fair to switch the rules for everybody who's still alive six months from today.

The Secure Act does have broad exceptions. Surviving spouses would be exempt from the accelerated payout. So would heirs who qualify as disabled or "chronically ill." For minor children (but not grandchildren), the 10-year timetable would start only after they hit the age of majority. Overall, most money in IRAs—about 3 in 4 dollars, according to congressional estimates—would be unaffected.

Yet the remaining 25% of IRA funds is hardly trivial. What's alarming, too, is how little attention this provision has received. The rules on retirement savings constitute a kind of social contract that shouldn't be hastily broken. Particularly as Social Security and Medicare slink toward insolvency, Congress may be tempted to fiddle with the laws on 401(k) plans and IRAs. It's a way for lawmakers to gin up revenue while pretending they aren't raising taxes. The political class wants more control over America's individual savings and investments.



The Secure Act has useful elements, but the Senate should find a different way to pay for it. Speeding up the taxes on heirs is a bad precedent. By all means Americans should keep paying into their retirement plans. But if this passes Congress, they might want to start sharpening their pitchforks.

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