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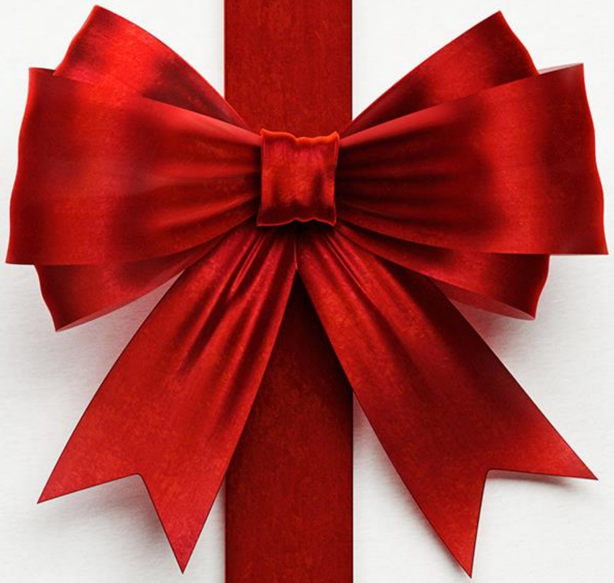

Understanding SECURE 2.0

Important Dates

Consolidated Appropriations Act, 2023

Passed Congress, Dec 23, 2022

Signed by President, Date of Enactment – Dec 29, 2022

Division T – SECURE Act 2.0

Expanding automatic enrollment in retirement plans

Section 101 requires 401(k) and 403(b) plans to automatically enroll participants in the respective plans upon becoming eligible (and the employees may opt out of coverage).

- The initial automatic enrollment amount is at least 3 percent but not more than 10 percent.
- Each year thereafter that amount is increased by 1 percent until it reaches at least 10 percent, but not more than 15 percent.
- **<u>All current 401(k) and 403(b) plans (plans established before Dec 29, 2022) are grandfathered</u>**.
- There is an exception for small businesses with 10 or fewer employees, new businesses (i.e., those that have been in business for less than 3 years), church plans, and governmental plans.

Effective for plan years beginning after December 31, 2024.

Expanding automatic enrollment in retirement plans

Beginning in 2025, many 403(b) plans will be subject to automatic enrollment.

This provision is <u>not</u> limited to 403(b) plans subject to ERISA.

Saver's Match

Current law provides for a nonrefundable credit for certain individuals who make contributions to individual retirement accounts ("IRAs") and employer retirement plans (401(k), 403(b) plans).

Section 103 repeals and replaces the credit with respect to IRA and retirement plan contributions, changing it from a credit paid in cash as part of a tax refund into a federal matching contribution that must be deposited into a taxpayer's IRA or retirement plan.

- The match is 50 percent of IRA or retirement plan contributions up to $2,000 per individual.
- The match phases out between:
  - $41,000 and $71,000 in the case of taxpayers filing a joint return,
  - $20,500 to $35,500 for single taxpayers and married filing separate;
  - $30,750 to $53,250 for head of household filers.

Section 103 is effective for taxable years beginning after December 31, 2026.

Saver’s Match

Where does the match come from?

- “Payable by the Secretary (of the Treasury) as soon as practicable after the eligible individual has filed a tax return making a claim for such matching contribution for the taxable year”

Where does the match go?

- To the “applicable retirement savings vehicle” chosen by the participant.
  - 401(k), 403(b), 457(b), IRA
  - Plan may choose not to accept the Saver’s Match
  - If amount under $100, participant can take as a credit
- Fully vested
- Not subject to statutory limits or nondiscrimination testing, e.g., 402(g), 415, ADP, Top heavy

MEP and PEP 403(b) plans

Multiple employer plans ("MEPs") provide an opportunity for small employers to band together to obtain more favorable retirement plan investment results and more efficient and less expensive management services.

Section 106 allows 403(b) plans to participate in MEPs and PEPs, including relief from the one bad apple rule so that the violations of one employer do not affect the tax treatment of employees of compliant employers.

Section 106 is effective for plan years beginning after December 31, 2022.

Increase in age for required beginning date for mandatory distributions

- Under current law, participants are generally required to begin taking distributions from their retirement plans at age 72.
  - The policy behind this rule is to ensure that individuals spend their retirement savings during their lifetime and not use their retirement plans for estate planning purposes to transfer wealth to beneficiaries.
  - The SECURE Act of 2019 increased the required minimum distribution age to 72.
- Section 107 further increases the required minimum distribution age further to 73 starting on January 1, 2023 – and increases the age further to 75 starting on January 1, 2033.

Increase in age for required beginning date for mandatory distributions

Date of birth	Required beginning date (Apr 1st following year)
7/1/1949 – 12/31/1950	Age 72
1/1/1951 – 12/31/1959	Age 73
On or after 1/1/1959*	Age 75
*This is a “glitch”. The way Act reads now, someone born in 1959 has two RMD ages: 73 and 75. This will have to be corrected.	

Reduction in excise tax on certain accumulations in qualified retirement plans on MRD failures

Section 302 reduces the penalty for failure to take required minimum distributions from 50 to 25 percent.

Further, if a failure to take a required minimum distribution from an IRA is corrected in a timely manner, as defined under this Act, the excise tax on the failure is further reduced from 25 percent to 10 percent.

Section 302 is effective for taxable years beginning after the date of enactment of this Act.

Individual retirement plan statute of limitations for excise tax on MRD failures

Under current law, the statute of limitations for excise taxes imposed on MRD failures starts running as of the date that Form 5329 is filed for the violation.

- Individuals often are not aware of the requirement to file Form 5329, and this can lead to an indefinite period of limitations that can cause hardship for taxpayers due to the accumulation of interest and penalties (see Paschall v. C.I.R., 137 T.C. 8 (2011)).
- In order to provide finality for taxpayers in the administration of these excise taxes, Section 313 provides that a 3-year period of limitations begins when the taxpayer files an individual tax return (Form 1040) for the year of the violation.
- In general, this change is intended to ensure that there is a reasonable period of limitations for violations of which taxpayers were not aware and thus did not file an excise tax return.

Section 313 is effective on the date of enactment of this Act.

Higher catch-up limit to apply at age 60, 61, 62, & 63

Under current law, employees who have attained age 50 are permitted to make catch-up contributions under a retirement plan in excess of the otherwise applicable limits. The limit on catch-up contributions for 2023 is $7,500.

Section 109 increases these limits to the greater of $10,000 or 50 percent more than the regular catch-up amount in 2025 for individuals who have attained ages 60, 61, 62 and 63.

- The increased amounts are indexed for inflation after 2025.

Section 109 is effective for taxable years beginning after December 31, 2024.

Treatment of student loan payments as elective deferrals for purposes of matching contributions

- Intended to help employees who may not be able to save for retirement because they are overwhelmed with student debt, and thus are missing out on available matching contributions for retirement.

- Permits an employer to make matching contributions under a 401(k) plan, 403(b) plan, or SIMPLE IRA with respect to “qualified student loan payments.”
  - A qualified student loan payment is broadly defined as any indebtedness incurred by the employee solely to pay qualified higher education expenses of the employee (not the employee’s children).
  - Employee must annually certify student loan payment; Employer may rely on certification.
  - Governmental employers are also permitted to make matching contributions in a section 457(b) plan or another plan with respect to such repayments.

Treatment of student loan payments as elective deferrals for purposes of matching contributions

If plan matches student loan payments, do so at same rate as match on elective deferrals

- Add deferrals and loan repayments.

Plan may treat student loan payment as an elective deferral for purposes of safe harbor, QACA or SIMPLE plans

Effective for plan years beginning after December 31, 2023

Nontrade or business SEP contributions

Section 118 permits employers of domestic employees (e.g., nannies) to provide retirement benefits for such employees under a Simplified Employee Pension (“SEP”).

Section 118 is effective for taxable years beginning after date of enactment of this Act.

Coverage for long-term part-time (“LTPT”) workers

The SECURE Act 1.0 requires employers to allow long-term, part-time workers to participate in the employers’ 401(k) plans.

SECURE Act 1.0 provides that – except in the case of collectively bargained plans – employers maintaining a 401(k) plan must have a dual eligibility requirement under which an employee must complete either 1 year of service (with the 1,000-hour rule) or 3 consecutive years of service (where the employee completes at least 500 hours of service).

SECURE Act 2.0 reduces the 3 year rule to 2 years, effective for plan years beginning after December 31, 2024.

Pre-2021 service is disregarded for vesting purposes, just as such service is disregarded for eligibility purposes under current law, effective as if included in the SECURE Act to which the amendment relates.

Coverage for long-term part-time (“LTPT”) workers

2024 plan year – apply SECURE 1.0 rules

3-year eligibility rule

Example

Plan year beginning 1/1/2024, must cover LTPT employees who have completed 3 years of service (500 – 999 hours)

- Count hours of service during 2021, 2022 and 2023

2025 plan year – apply new SECURE 2.0 rules

2-year eligibility rule

Example

Plan year beginning 1/1/2025, must cover LTPT employees who have completed 2 years of service (500 – 999 hour)

- Count hours of service during 2023 and 2024

Coverage for long-term part-time ("LTPT") workers

This provision also extends the long-term part-time coverage rules to 403(b) plans that are subject to ERISA.

Appears to supersede both the 20-hours-per-week and student-employee exemptions.

We have two more years before the rule is effective for 403(b) plans. Hopefully, the IRS will publish a clarification.

Emergency savings accounts in individual account plans

- Once the cap is reached, the additional contributions can be directed to the employee’s Roth defined contribution plan (if they have one) or stopped until the balance attributable to contributions falls below the cap.
- Contributions are made on a Roth basis and are treated as elective deferrals for purposes of retirement matching contributions with an annual matching cap set at the maximum account balance – i.e., $2,500 or lower as set by the plan sponsor.
- Match goes into match account (not ESA).
- The first four withdrawals from the account each plan year may not be subject to any fees or charges solely on the basis of such withdrawals.
- At separation from service, employees may take their emergency savings accounts as cash or roll it into their Roth defined contribution plan (if they have one) or IRA.
- NHCEs only. If NHCE becomes an HCE, no further contributions to ESA.
- Investment limited to capital preservation or interest-bearing account.

Enhancement of 403(b) plans – CITs

Under current law, 403(b) plan investments are generally limited to annuity contracts and publicly traded mutual funds.

This limitation cuts off 403(b) plan participants – generally, employees of charities and public schools, colleges, and universities– from access to collective investment trusts, which are often used by 401(k) plans to expand investment options for plan participants at a lower overall cost.

Section 128 would permit 403(b) custodial accounts to participate in group trusts with other tax-preferred savings plans and IRAs, and would be effective after date of enactment

Enhancement of 403(b) plans – CITs

Revisions to the securities laws are required to permit 403(b) plans to invest in CITs.

Higher dollar limit for mandatory distributions

- Under current law, employers may transfer former employees' retirement accounts from a workplace retirement plan into an IRA if their balances are between $1,000 and $5,000.

- Last changed in 1997.

- Section 307 increases the limit from $5,000 to $7,000 (not indexed), effective for distributions made after December 31, 2023.

Expansion of Employee Plans Compliance Resolution System

Because of the ever-growing complexity of retirement plan administration, Section 305 expands the Employee Plans Compliance Resolution System ("EPCRS") to

- Allow more types of errors to be corrected internally through self-correction,
- Apply to inadvertent IRA errors, and
- Exempt certain failures to make required minimum distributions from the otherwise applicable excise tax.

For example, Section 305 allows for correction of many plan loan errors through self-correction, which are a frequent area of error and can be burdensome to correct a single loan error through the Internal Revenue Service.

Section 305 is effective on the date of enactment of this Act.

Any guidance or revision of guidance required by Section 305 shall be promulgated no later than 2 years after the date of enactment of this Act.

Revenue Procedure 2021–30 (or any successor guidance) shall be updated to take into account the provisions of this section no later than 2 years after the date of enactment of this Act.

Application of top heavy rules to defined contribution plans covering excludable employees

Plans that are deemed top-heavy are required to provide employees with a minimum of a 3 percent of pay nonelective contribution.

Other nondiscrimination tests that apply to 401(k) plans allow an employer to test otherwise excludable employees (e.g., those who are under age 21 and have less than 1 year of service) separately.

- This was intended to encourage plan sponsors to permit employees to defer earlier than the minimum age and service conditions permitted under the law because it reduces the situations where plans would fail the nondiscrimination tests if these employees were included when performing the test.
- However, this separate testing is not allowed for the top-heavy test. As a consequence, small employer retirement plans often do not cover excludable employees because, if the plan is or becomes top heavy, the employer ise required to contribute the top- heavy employer contribution for all employees who are eligible to participate in the plan.
- Section 310 allows an employer to perform the top-heavy test separately on the non-excludable and excludable employees.
- This removes the financial reason to exclude employees from the 401(k) plan.

Section 310 is effective for plan years beginning after December 31, 2023.

Employer may rely on employee certifying that deemed hardship distribution conditions are met

Employees are permitted to self-certify that they have had an event that constitutes a hardship for purposes of taking a hardship withdrawal.

Distribution is on account of immediate and heavy financial need under safe harbor regulations

Distribution does not exceed the amount of need

Employee does not have other resources

Current hardship rules already permit employees to self-certify that they do not have other funds available to address a hardship.

Section 312 is effective for plan years beginning after the date of enactment of this Act.

Hardship distributions from 403(b) plans

Allows 403(b) hardship distributions to be administered same as 401(k) hardships.

- Deferrals
- QNECs, QMACs, Safe Harbor contributions
- Earnings

No requirement to take loan first.

Hardship Verification

Plan now has 3 choices

1. **Get copies of documents showing existence of hardship and amount**
   - Only option for non-safe harbor hardships
2. **IRS summary verification system (substantiation guidelines)**
   - Sponsor must provide information re: hardship rules to participant
   - Sponsor must obtain summary information from the participant
   - Participant required to retain source documents
3. **New: Participant certifies existence of hardship and amount**
   - I need a $5,000 hardship distribution to cover medical expenses for my kid

Amendment to increase benefits under plan for previous plan year allowed until employer tax return due date

Current law provides that plan amendments must generally be adopted by the last day of the plan year in which the amendment is effective.

This precludes an employer from adding plan provisions that may be beneficial to participants.

Section 316 allows discretionary amendments that increase participants' benefits to be adopted by the due date of the employer's tax return.

Section 316 is effective for plan years beginning after December 31, 2023.

Use of retirement funds in connection with qualified federally declared disasters

Section 331 provides permanent rules relating to the use of retirement funds in the case of a federally declared disaster.

The permanent rules allow up to $22,000 to be distributed from employer retirement plans or IRAs for affected individuals.

- Such distributions are not subject to the 10 percent additional tax and are taken into account as gross income over 3 years.
- Distributions can be repaid to a tax-qualified retirement account.
- Amounts distributed prior to the disaster to purchase a home can be recontributed, and an employer is permitted to provide for a larger amount to be borrowed from a plan by affected individuals and for additional time for repayment of plan loans owed by affected individuals.

Section 331 is effective for disasters occurring on or after January 26, 2021.

Employers allowed to replace SIMPLE retirement accounts with safe harbor 401(k) plans during a year

Under current law, the employer is stuck with the SIMPLE IRA for entire year.

Section 332 allows an employer to replace a SIMPLE IRA plan with a Safe Harbor 401(k) plan that requires mandatory employer contributions during a plan year.

- SIMPLE 401(k), QACA, or Safe Harbor plans

Deferral dollar limit is prorated (by days) between SIMPLE and 402(g) dollar limits

Effective for plan years beginning after December 31, 2023.

Rollover from SIMPLE IRA to 401(k) or 403(b)

- Typically, cannot roll from SIMPLE IRA to plan in first two years of participation (no issue for SEP IRA rollovers)

- If employer terminates SIMPLE IRA and establishes 401(k) or 403(b), can roll from SIMPLE to plan, if rollover is subject to 401(k)/403(b) distribution restrictions

- Not limited to midyear conversions

Safe harbor for corrections of employee elective deferral failures

Under current law, employers that adopt a retirement plan with automatic enrollment and automatic escalation features could be subject to significant penalties if mistakes are made.

The Internal Revenue Service has issued guidance on the correction of failures relating to default enrollment of employees into retirement plans.

This guidance includes a safe harbor, which expires December 31, 2023, that permits correction if notice is given to the affected employee, correct deferrals commence within certain specified time periods, and the employer provides the employee with any matching contributions that would have been made if the failure had not occurred.

Employers are concerned about the lapse of the safe harbor at the end of 2023.

Section 350 allows for a grace period to correct, without penalty, reasonable errors in administering these automatic enrollment and automatic escalation features.

Errors must be corrected prior to 9 ½ months after the end of the plan year in which the mistakes were made.

Section 350 is effective to errors after December 31, 2023.

Catch up contributions must be Roth

Under current law, catch-up contributions to a qualified retirement plan can be made on a pre-tax or Roth basis (if permitted by the plan sponsor).

Section 603 provides all catch-up contributions to qualified retirement plans are subject to Roth tax treatment, effective for taxable years beginning after December 31, 2023.

An exception is provided for employees with prior year "FICA wages" of $145,000 or less (indexed).

Catch up contributions must be Roth

When Congress changed catch-up rules for HCE, they amended out the income exclusion for all pre-tax catch-up contributions

We (and everyone else) expect this will be part of technical corrections bill in near future…

Optional treatment of employer matching or nonelective contributions as Roth contributions

Under current law, plan sponsors are not permitted to provide employer matching or nonelective contributions in their 401(k), 403(b), and governmental 457(b) plans on a Roth basis.

Matching and nonelective contributions must be on a pre-tax basis only.

Section 604 allows defined contribution plans to provide participants the option of receiving matching or nonelective contributions on a Roth basis.

Presumably follow rules for Roth deferrals.

Effective on the date of enactment of this Act.

Provisions relating to plan amendments

1

Plan amendments made pursuant to this Act must be made on or before the last day of the first plan year beginning on or after January 1, 2025 (2027 in the case of governmental plans).

2

The plan must operate in accordance with such amendments as of the effective date of the amendment.

3

Section 501 also conforms the plan amendment dates under the SECURE Act, the CARES Act, and the Taxpayer Certainty and Disaster Tax Relief Act of 2020 to these new dates (instead of 2022 and 2025).

Change in Participant Count for Plan Audit Threshold

1

What's the new rule?

- Generally, plans with fewer than 100 participants can use simplified Form 5500 reporting – most notably the plan does not have to be audited by an independent qualified public accountant.
- Rather than counting all participants that are either eligible or have an account balance, the new rule counts only the number of participants and beneficiaries with account balances at the beginning of the plan year.

2

What's the impact?

- DOL expects this change to reduce the number of plans that must file as large plans by nearly 19,500 filers.

3

When is the new rule effective?

- Plan years beginning on or after Jan 1, 2023.
- Filing and audit requirements for 2022 plan years determined based on prior counting rules.

District Court Vacates DOL "Investment Advice" Definition

DOL five-part definition of "investment advice" – A person provides "investment advice" if he/she:

- Makes recommendations as to the advisability of investing in, purchasing, or selling securities or other property;
- On a "regular basis";
- Pursuant to a mutual understanding;
- That such advice will be a primary basis for investment decisions; and
- The advice will be individualized to the plan.

In PTE 2020-02, which allows "conflicted" advice arrangements, the DOL stated that when an advisor has not previously provided advice but expects to regularly make investment recommendations with respect to an IRA as part of an ongoing relationship, a recommendation to roll assets out of an ERISA plan into an IRA would satisfy the "regular basis" prong.

Thus, an initial recommendation without a prior relationship can satisfy the five-part test.

District Court Vacates DOL "Investment Advice" Definition

American Securities Ass'n v. US Department of Labor (M.D. Fla. Feb 13, 2023) – DOL's interpretation of "regular basis" prong is unreasonable and arbitrary.

- ERISA statutory text and 1975 regulation define fiduciary investment advice as advice given "to a particular plan."
- The court reasoned that in the context of a rollover, any investment advice given after the rollover is "inheritantly divorced from the ERISA-governed plan".
- Because DOL interpretation combines advice given to the plan with advice given post-rollover, the court vacated DOL interpretation (see FAQ 7 of 2021 FAQs).

Implications

- Court did not discuss scenario where adviser has been providing investment recommendations to the plan.
- DOL has included a fiduciary investment advice regulation on its regulatory agenda.

IRS Sets Deadline for Using Plan Forfeitures

On February 27, 2023, the IRS issued proposed regulations imposing a deadline for when a defined contribution plan (like a 401(k) plan) must use forfeitures to pay plan expenses, reduce employer contributions or reallocate to participant accounts.

The deadline is 12 months following the close of the plan year in which forfeitures are incurred under the plan terms.

- This rule is the formalization of informal positions taken by both the IRS in previous guidance and the U.S. Department of Labor in its more recent audit activities.

This new rule is effective for plan years beginning on or after January 1, 2024.

- To provide transition relief, the rule provides that all forfeitures incurred during plan years beginning before January 1, 2024 will be treated as having been incurred in the first plan year that begins on or after January 1, 2024.
- For plan sponsors that have been accumulating forfeitures, this means those forfeitures will need to be used by the end of the 2025 plan year.

Thank you!